Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
The Library of Congress
Washington, D.C.

In re **DETERMINATION OF ROYALTY RATES AND TERMS FOR MAKING AND DISTRIBUTING PHONORECORDS (Phonorecords III)**	**Docket No. 16–CRB–0003–PR (2018–2022) (Remand)**

SERVICES' JOINT REPLY BRIEF

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Amazon.com Services LLC, Google LLC, Pandora Media, LLC, and Spotify USA Inc. (collectively, the "Services") respectfully submit this joint reply brief in support of their revised proposal for rates and terms for the 2018-2022 period (the "Services' Proposal"[1]) and in opposition to the Copyright Owners' proposal.

INTRODUCTION

The D.C. Circuit's *Johnson* decision requires the Judges to take a fresh look at the evidence and adopt rate levels and a rate structure that are reasonable and satisfy all four statutory factors under Section 801(b)(1). The Services have offered a rate proposal that satisfies those factors. That proposal is grounded in the *Phonorecords II* framework, which has a proven track record of supporting mutually beneficial industry growth, and includes modest modifications to address more recent service offerings.

The Copyright Owners, in contrast, have not even *tried* to explain how their proposal satisfies all four statutory factors. As the Services have shown, that proposal must be rejected because, among other reasons, it is based on a false premise. In adopting the vacated rates and rate structure, the Majority made the "heroic assumption" that raising mechanical rates would have a "see-saw" effect because record labels would voluntarily reduce sound recording royalties in response to increasing mechanical royalties and "accept millions of dollars in lost revenue." *Determination of Royalty Rates and Terms for Making and Distributing Phonorecords* (*Phono III*), Final Rule, 84 Fed. Reg. 1918, 1966 (Feb. 5, 2019) (Dissent) (cleaned up). That assumption, which was unsupported and flawed from the outset, has now been decisively disproven in the marketplace. After the Majority increased mechanical royalty rate levels and uncapped the total content cost ("TCC") prong for all offerings, record labels did not voluntarily

[1] The Services' Proposal was submitted with the Services' Joint Opening Brief.

reduce sound recording royalties—indeed, they refused to do so [redacted]. Instead, the Services were forced to bear significant increases in mechanical royalties without any offsetting reduction in sound recording royalties.

Unable to offer a serious defense of their proposal, the Copyright Owners urge the Judges rely on the "same . . . reasoning" from the Final Determination and to re-adopt the vacated rate levels and rate structure. Copyright Owners' Br. at 37. They contend that the Judges can conclude that the vacated rate levels and rate structure are appropriate because they did not cause an immediate catastrophe for the streaming industry. But, as *Johnson* made clear, the Judges must provide a reasoned explanation why their chosen approach appropriately balances all four statutory factors. To re-impose the Final Determination's rate levels and structure on the sole ground they had not been sufficiently disruptive before the D.C. Circuit vacated them (and before the full rate increase took hold) would be a clear abdication of that duty and would be arbitrary and capricious. *See Pub. Citizen v. Fed. Motor Carrier Safety Admin.*, 374 F.3d 1209, 1216, 1223 (D.C. Cir. 2004) (vacating agency decision as "arbitrary and capricious" where the "agency neglected to consider a statutorily mandated factor"). Tellingly, the Copyright Owners identify no instance where an agency has *ever* reinstated a rate that the D.C. Circuit vacated simply because there has not been a catastrophic consequence in the interim, as they urge the Judges to do here.

The Copyright Owners' arguments in favor of readopting the vacated rates instead of the Services' proposal based on the *Phonorecords II* settlement fail for four reasons:

First, the Copyright Owners misconstrue *Johnson*, which explained that, on remand, the Judges would need to engage in a new analysis to select rate levels and a rate structure that are reasonable and satisfy all four statutory factors. For that reason, the court declined to address the

Services' arguments as to three of the four statutory factors, as well as the question whether substantial evidence supported the Majority's "see-saw" theory. *See Johnson v. Copyright Royalty Bd.*, 969 F.3d 363, 383, 388-89 (D.C. Cir. 2020). The Copyright Owners are wrong to suggest that *Johnson* endorsed the rate levels and rate structure they seek to re-impose. To the contrary, the D.C. Circuit pointedly described the vacated determination as "yok[ing]" mechanical royalties to record labels' "unchecked market power" and making an "extreme change" to mechanical royalty rate levels. *Id.* at 382. That language implies serious substantive concerns with the Judges' prior decision—and, at a minimum, precludes the Judges from simply re-imposing those same rate levels and rate structure without careful scrutiny. *See* Part I.

Second, the Copyright Owners offer no cogent explanation for why the Judges should disregard the *Phonorecords II* settlement, which bears all of the hallmarks of an appropriate benchmark. They also fail to address the proven success of the *Phonorecords II* settlement. For years, the *Phonorecords II* rate structure and rate levels supported market growth that benefited the Copyright Owners and the Services; as the Services drew new customers to interactive streaming, royalty payments rose. Instead, they resort to blatantly mischaracterizing the D.C. Circuit's *Johnson* decision as affirming the rejection of the *Phonorecords II* benchmark—when, in fact, the court did the opposite—and re-assert a series of arguments that the Judges have already rejected. *See* Part II.

Third, the Copyright Owners fail to show that the vacated rates and rate structure they urge the Judges to re-adopt satisfy the Section 801(b)(1) factors. Indeed, they make only fleeting references to those factors. But the D.C. Circuit left no doubt that the Judges must consider all four factors during this remand because they are "intertwined" with the selection of the final rate levels and rate structure. *Johnson*, 969 F.3d at 389. By neglecting to address those factors, the Copyright Owners offer no serious defense of their own proposal. *See* Part III.

Fourth, the Copyright Owners do not identify any source of statutory authority that would allow the Judges to revise the Initial Determination's definition of Service Provider Revenue. Indeed, their only discussion of this threshold issue appears in a single footnote, betraying the weakness of their argument. *See* Part IV.

In sum, the Copyright Act requires the Judges to select rates and a rate structure that are reasonable, will maximize the availability of creative works to the public, afford both the Copyright Owners and Services a fair income, reflect their relative roles in making creative works available to the public, and minimize disruption in the interactive music streaming industry. Only the Services have put forward a proposal that will balance all of those interests, enable the interactive streaming industry to continue growing, and thereby sustain the upward trajectory of mechanical royalty payments. The Judges should adopt that proposal and reject the Copyright Owners' invitation to re-adopt flawed rates based on a debunked premise.

ARGUMENT

I. THE D.C. CIRCUIT'S DECISION IN *JOHNSON* REQUIRES THE JUDGES TO DETERMINE THE RATE LEVELS AND RATE STRUCTURE THAT BEST COMPORT WITH THE GOVERNING SECTION 801(b)(1) STANDARD

A. The *Johnson* Decision Requires Revisiting Essential Components of the Final Determination

The D.C. Circuit vacated the Final Determination because of both its procedural and substantive flaws. And the D.C. Circuit's directives for this remand were clear: The Judges must reevaluate their previous determinations and adopt rate levels and a rate structure that serve all the objectives in the Copyright Act. As the court explained, the Final Determination took the "dramatic step" of "pair[ing] . . . significant increases in the total content cost and revenue prongs" with "uncapping the total content cost prong for every category of service offering." *Johnson*, 969 F.3d at 381. And the Majority "failed to provide adequate notice of the drastically modified rate structure it ultimately adopted." *Id.* That failure was "no mere formality" because it deprived the parties of the "ability to provide evidence and argument bearing on the essential components and contours of the Board's ultimate decision." *Id.* The parties were deprived of notice with respect to *both* the decision to "strip[] away the total content cost caps" and the decision to "significantly hike[] . . . the revenue rate and the total content cost rates." *Id.* at 382-83. Because the parties had no opportunity to test the combination of rate levels and rate structure that the Board selected, there was no assurance that "the Board's ultimate decision [was] well-reasoned and grounded in substantial evidence." *Id.* at 381.

The D.C. Circuit raised other substantive concerns about the rate levels and rate structure the Majority adopted. The court emphasized that the Majority failed to conduct a "reasoned analysis" of whether the *Phonorecords II* settlement was an appropriate benchmark. *Id.* at 387. And the court critiqued the Majority's decisions to "yoke[] the mechanical license royalties to the sound recording rightsholders' unchecked market power," to "remove[] the only structural limitation on how high the total content cost (which is pegged to unregulated sound recording royalties) can climb" by eliminating the TCC caps across the board, and to "also significantly hike[] both the revenue rate and the total content cost rates the streaming services would have to pay." *Id.* at 380, 382-83. The "end result," the court pointedly noted, was an "extreme change" in the rate levels and rate structure that "could significantly increase costs for the Streaming Services." *Id.* at 382.

In light of the vacatur, the D.C. Circuit decided that it "need not address" many of the Services' other challenges to the Final Determination, leaving the Board to consider those issues on remand. *Id.* at 383. These open issues include whether the Majority "failed to provide a 'satisfactory explanation,' or root in substantial evidence, its conclusion that an increase in mechanical license royalties would lead to a decrease in sound recording royalties." *Id.* They also include the Services' contention that the Majority did not "adequately address[ ] factors B through D," including that the Majority "failed to consider whether interactive streaming services would receive fair revenue under the rates and rate structure it adopted." *Id.* at 388-89.

As to each of those unresolved challenges, the D.C. Circuit recognized that the Judges would need to evaluate them anew on remand. For example, the court explained that the "Services can present their concerns" about the lack of evidentiary support for the "see-saw" hypothesis "to the Board in the first instance." *Id.* at 383. And as to factors B through D, the court recognized that the proper analysis "is intertwined with the nature of the rate structure ultimately imposed" on remand and the Judges' further "analysis of sound recording rightsholders' likely responses to the new rate structure." *Id.* at 389.

B. The Copyright Owners Mischaracterize *Johnson*

Despite the D.C. Circuit's clear rulings, the Copyright Owners attempt to rewrite *Johnson* in support of their effort to convince the Judges to reinstate the rate levels and rate structure that the D.C. Circuit vacated. Those efforts fail.

1. The Copyright Owners first argue (at 1) that "this remand is limited to *three discrete issues*." As shown above, however, the issues that the Judges must decide on remand are not "discrete" (or narrowly "limited"). The D.C. Circuit explicitly stated that numerous questions going to both the rate levels and the rate structure—including the evidentiary basis of the see-saw theory, the appropriateness of the *Phonorecords II* settlement as a benchmark, and the proper analysis of the statutory factors—remain for the Judges to address on remand. *Johnson*, 969 F.3d at 383, 387, 389. While the Copyright Owners cite the Judges' Order

Regarding Proceedings on Remand in support of this claim, that Order contained only a high-level summary of the issues that would be decided on remand and was not, as the Copyright Owners appear to believe, a complete encapsulation of the open issues. *See* Order Regarding Proceedings on Remand at 1, *Phono III*, No. 16-CRB-0003-PR (2018-2022), eCRB Doc. No. 23390 (Dec. 15, 2020).[2] And in any event, that Order cannot alter the scope of the D.C. Circuit's remand. The D.C. Circuit's decision makes clear that the Judges *must* reconsider the "drastically modified rate structure" and "significantly increased rates" that the Majority adopted. *Johnson*, 969 F.3d at 381. It would be clear error for the Judges to ignore the scope of the D.C. Circuit's decision and artificially circumscribe the issues on remand. Indeed, it would once again deprive the Services of a full opportunity to make their case. The Judges should reject the Copyright Owners' effort to limit the scope of this proceeding.

2. Next, the Copyright Owners contend (at 10) that the D.C. Circuit vacated the Majority's decision to reject the *Phonorecords II* settlement as a benchmark "merely" so that the Judges can provide a new "reasoned analysis" for rejecting the benchmark. But the D.C. Circuit would not have vacated the "rate structure and percentages" if it only intended for the Judges to provide a fuller explanation of the prior determination. *Johnson*, 969 F.3d at 381. If the court believed that "there [was] at least a realistic possibility that [the Judges would] be able to substantiate the [Final Determination] on remand," the court could have remanded for such

[2] In their proposal for the remand proceedings, the Services stated that "the D.C. Circuit unanimously identified three errors in the *Phonorecords III* Final Determination that led it to vacate that decision," but never suggested that the scope of the remand was limited to the errors that led to the vacatur or that those were the only issues the Judges needed to address on remand. Services' Proposal for Remand Proceedings at 3, *Phono III*, No. 16-CRB-0003-PR (2018-2022), eCRB Doc. No. 23383 (Dec. 10, 2020). Rather, the Services emphasized that the court "also left open" other issues, including "whether the Board's 'conclusions with respect to the four statutory [Section 801(b)(1)] objectives were unreasoned and unsupported by substantial evidence.'" *Id.* at 2 (quoting *Johnson*, 969 F.3d at 384).

substantiation without vacating. *Clean Wisc. v. EPA*, 964 F.3d 1145, 1177 (D.C. Cir. 2020); *see also, e.g.*, *Allied-Signal, Inc. v. U.S. Nuclear Regul. Comm'n*, 988 F.2d 146, 150-51 (D.C. Cir. 1993). But that is not what the court did. It *vacated* the rate structure and rate levels and directed the Judges to conduct "a reasoned analysis" of the benchmark as a whole—not simply to provide a reasoned analysis of why it previously rejected the benchmark. *Johnson*, 969 F.3d at 381, 387. As a result, the Judges must reassess the broader question of whether the benchmark is useful and comports with the governing rate-setting standard. (The Dissent, of course, found that benchmark highly probative.)

Relatedly, and contrary to the Copyright Owners' suggestions (at 2), the D.C. Circuit did *not* endorse any of the arguments for rejecting the *Phonorecords II* benchmark that the Board's appellate counsel raised for the first time. Nor did the D.C. Circuit indicate that those justifications were supported by the record. The court never "affirmed the Board's conclusion that the *Phonorecords II* rates were too low" and never "approved of" the Majority's "analysis of the expert evidence in the record underpinning the Board's rate increase" as the Copyright Owners erroneously contend (at 13). In fact, the D.C. Circuit did the *opposite*. It said that the idea that the *Phonorecords II* rates "had been set far too low" was "nowhere to be found in the Final Determination's discussion of the appropriateness of the Phonorecords II settlement as a potential benchmark." *Johnson*, 969 F.3d at 387. And the court explained that, under basic administrative law principles, it was limited to assessing the validity of the Final Determination based on the reasons in that decision. *Id.*

Nor did the court affirm (much less embrace) the specific percentages that the Majority derived from the mixed and matched economic models or examine them in light of the Section 801(b)(1) factors. *See id.* at 384-89. On the contrary, the court held that whether the Majority's rate levels and rate structure satisfy the statutory rate-setting standard is "bound up" with "the nature of the rate structure ultimately imposed [on remand] by the Board." *Id.* at 389. Thus, the court declined to reach the merits of the issues that the Copyright Owners now mistakenly claim have already been resolved. *Id.* Those remain open issues on remand.

Further, even though the court indicated that there was some basis in the record for the Majority's conclusion that increasing royalty rates would help "maximiz[e] the availability of creative works" under factor A, the D.C. Circuit expressly declined to "address whether the Board adequately considered" the other three statutory factors. *Id.* at 387-89. The Copyright Owners once again ask the Judges to ignore factors B and C and determine that, because increasing royalties would serve the Copyright Owners' (short term) interests, the Judges need not consider whether such an increase would, say, provide a fair income to the Services or appropriately credit their relative contributions, investments, and risks. That is not what the D.C. Circuit said. The court, consistent with the governing statute, unambiguously stated that the Judges must consider whether the rates serve all "four statutory objectives." *Id.* at 387.[3]

3. The Copyright Owners also erroneously assert (at 36-37) that the D.C. Circuit vacated the rate structure and rate levels "merely . . . because it believed the Services 'were procedurally blindsided,'" and thus, the Board can simply "maintain[ ] the TCC prong it adopted" previously, based on the same reasoning in the Final Determination, so long as "the Services are provided an opportunity to 'voice their objections'" in this remand proceeding.

[3] *See also Music Choice v. Copyright Royalty Bd.*, 774 F.3d 1000, 1013 (D.C. Cir. 2014) (explaining that "'reasonable rates' are those that are calculated with reference to the four statutory criteria" (citation omitted)); *Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd.*, 684 F.3d 1332, 1339 (D.C. Cir. 2012) (noting that royalty rates must "serve all these objectives adequately" (citation omitted)); *Recording Indus. Ass'n of Am. v. Libr. of Cong.*, 176 F.3d 528, 533 (D.C. Cir. 1999) (stating that "rates are to 'be calculated to achieve' the four objectives of § 801(b)(1)").

Though the D.C. Circuit held that the Services did not have a sufficient opportunity to challenge the rate levels and rate structure that the Majority ultimately selected, simply allowing the Services an opportunity to be heard is not enough. Instead, to comply with the D.C. Circuit's directives, the Judges must address the substantive issues raised by the Services on remand, including the threshold issue of whether evidence supports the "see-saw" theory undergirding the Majority's rate determination.

The Majority rested its Final Determination on the "heroic assumption" that record labels would voluntarily "accept millions of dollars in lost revenue" by agreeing to "lower sound recording royalties" in response to an increase in mechanical rates. *Phono III*, 84 Fed. Reg. at 1966 (Dissent); *see also Phono III*, 84 Fed. Reg. at 1953 ("[T]he Judges rely on Professor Watt's insight (demonstrated by his bargaining model) that sound recording royalty rates in the unregulated market will decline in response to an increase in the compulsory license rate for musical works."). This see-saw theory was central to the Majority's decision to transform the rate structure and dramatically raise the rate levels, and it allowed the Majority to avoid the implications that the novel rate structure and the steep rate increase would have on the Services under factors B through D. *See Johnson*, 969 F.3d at 372, 389. Indeed, the Majority assumed that uncapping the TCC prong and raising the rate levels would not ultimately affect the Services' bottom lines because the Services would simply "adapt to the changed circumstance" by successfully negotiating lower sound recording royalty rates. *Phono III*, 84 Fed. Reg. at 1953, 1958-60; *see also id.* at 1966-67. This reasoning ignored the well-established complementary oligopoly power of the record labels and their resistance to voluntarily foregoing millions of dollars of revenue.

More to the point, if the see-saw theory lacks evidentiary merit—and the evidence adduced on remand shows that it does, *see infra* Section III.B—then the justification for uncapping the TCC prong and raising the rate levels disappears. That is why the D.C. Circuit's affirmance of the Majority's findings regarding factor A does not and cannot suffice as a basis to reinstate the vacated rate levels and rate structure. The Judges still must assess whether the rate levels and rate structure they select on remand satisfy *all four* of the statutory factors, including affording "copyright users a fair income," "reflecting the relative roles of the copyright owners and users in making music available to the public," and "minimizing any disruption on the 'structure of the industries involved and on generally prevailing industry practices.'" *Johnson*, 969 F.3d at 387 (quoting 17 U.S.C. § 801(b)(1) (2012)).

4. Finally, the Copyright Owners argue (at 7-8) that the D.C. Circuit vacated the Majority's modification of the Service Provider Revenue definition for bundles simply because "the Board had provided an unclear or conflicted explanation of the procedural authority under which it revised the definition." To be clear, the D.C. Circuit did not think that explanation was just "unclear or conflicted." The court held that the Majority "completely failed to explain under what authority it was able to materially rework th[e] definition so late in the game." *Johnson*, 969 F.3d at 389-92.

In particular, "[t]he Board's material revision of the 'Service Revenue' definition for bundled offerings [did] not fall within the Board's rehearing authority under Section 803(c)(2)(A)" because the Majority was "explicit that it did not treat the [Copyright Owners'] motion[ ] to have the definition changed as [a] motion[ ] for rehearing." *Id.* (citation omitted). The court also noted that the Majority had not given any indication that its decision to modify the definition was "an exercise of its authority under Section 803(c)(4) to 'correct any technical or clerical errors in the determination.'" *Id.* at 391. "Quite the opposite," "the new definition represent[ed] a departure from the definition in the Initial Determination" and constituted "a substantive swap." *Id.* (citation omitted). "Nor did the Board's order purport to modify the terms in response to unforeseen circumstances that would frustrate the proper implementation of the Initial Determination" under Section 803(c)(4). *Id.* (cleaned up). Again, "[t]he order never mention[ed] Section 803(c)(4) or unforeseen circumstances as the basis for revamping the Service Revenue definition." *Id.*

The D.C. Circuit also declined to consider the justifications that the Board's appellate counsel raised for the first time on this issue, explaining that the court "may sustain agency action only for the reasons invoked by the agency at the time it took the challenged action." *Id.* at 390-91. In doing so, the court emphasized that any expanded or new justifications for revising the Initial Determination on remand needed to be consistent with the limits Congress had placed on the Judges' authority to revise their previous determinations. *Id.* at 392. And the court reiterated that the Majority had failed to "explain[ ] the source of its power to make 'fundamental' changes under the authorizing statute." *Id.* Thus, the Judges must first address a threshold question: whether they even have "any legal authority" to modify the definition in the Initial Determination. *Id.*

The Copyright Owners nonetheless assert (at 74) that the Judges can simply "take new agency action . . . to cure the asserted procedural defect." But the remand does not obviate the need for the Judges first to identify a source of authority that would allow them to modify the Initial Determination's definition, a threshold question that the Copyright Owners have relegated to a footnote. *See* Copyright Owners' Br. at 71 n.33. The only way the Judges can take "new agency action" on this issue is by locating some previously unidentified source of statutory authority for revising the Initial Determination's definition. But no such authority exists. *See infra* Section IV.A; *Johnson*, 969 F.3d at 390-92. The D.C. Circuit's acknowledgment that the Judges can take "new agency action" on remand does not give the Board the ability to bypass the threshold question of its authority to amend the Initial Determination. As the D.C. Circuit explained, the Judges may only exercise authority to revise an initial determination "within the lines drawn by the authorizing statute." *Johnson*, 969 F.3d at 392. Revising this aspect of the Initial Determination on remand in the absence of any statutory authority would directly conflict with "Congress's decision to limit rehearing to 'exceptional cases,' and to confine other *post hoc* amendments to cases involving 'technical or clerical errors.'" *Id.*

II. THE *PHONORECORDS II* SETTLEMENT SHOULD BE ADOPTED AS A BENCHMARK

The Copyright Owners' brief largely rehashes arguments against the *Phonorecords II* settlement that the Judges—both the Majority and Judge Strickler—already rejected. As the Services have explained, the *Phonorecords II* settlement bears all of the characteristics of an appropriate benchmark: it conveys the same rights at issue in this proceeding, it involves the same or similar buyers and sellers, and the key economic circumstances of the market have not changed since its execution. *See* Services' Br. at 19-34; *see also Phono III*, 84 Fed. Reg. at 1999 (Dissent). The Copyright Owners do not seriously dispute any of these points. Nor do they challenge the evidence demonstrating that the *Phonorecords II* agreement spurred extraordinary market growth and dramatically increased royalty payments to the Copyright Owners.

A. The *Phonorecords II* Rate Levels Are Not "Too Low"

The Copyright Owners spend much effort arguing that the *Phonorecords II* rates are "too low"—and even suggest that the D.C. Circuit blessed the argument. But the D.C. Circuit did not "affirm" that the *Phonorecords II* rates were too low; it declined to address that argument as it was nowhere to be found in the Final Determination. The Copyright Owners' other efforts to demonstrate that the *Phonorecords II* rates are "too low" are similarly misguided. Those rates allowed for market growth to the benefit of the Copyright Owners and are supported by reams of record evidence. The *Phonorecords II* rates are in line with the rate for digital downloads under subpart A that the Copyright Owners not only deemed reasonable in *Phonorecords III* but also have just recently reaffirmed through 2027 in *Phonorecords IV*. *Phono III*, 84 Fed. Reg. at 1947; Notice of Settlement in Principle, *In re Determination of Royalty Rates and Terms for Making and Distributing Phonorecords* (*Phono IV*), No. 21-CRB-0001-PR (2023-2027) (Mar. 2, 2021). They are consistent with the rates that numerous publishers agreed to in direct deals with the Services. *Phono III*, 84 Fed. Reg. at 1966 (Dissent); *see also* Ex. 885 ¶¶ 73-78 (Katz WDT). And they are consistent with the rates that emerge from an appropriately constructed Shapley model, like the one Professor Marx put forward.

1. The D.C. Circuit Did Not "Affirm" that the **Phonorecords II** *Rates Are Too Low*

The Copyright Owners are wrong (at 13) in claiming that the D.C. Circuit implicitly "affirmed" that the "*Phonorecords II* rates were too low." Instead, the D.C. Circuit found that the Majority had *not* relied on the rates being "too low" as a reason for rejecting the *Phonorecords II* settlement as a benchmark, that the argument was made for the first time on appeal (by the Government, not the Copyright Owners), and that the argument was "nowhere to be found in the Final Determination." *Johnson*, 969 F.3d at 387. Far from "affirm[ing] the Board's conclusion that the *Phonorecords II* rates were too low," Copyright Owners' Br. at 13, the D.C. Circuit made clear that the Majority had never reached such a "conclusion." And by vacating the Majority's chosen rates, the D.C. Circuit left open whether the Judges should adopt the *Phonorecords II* rates on remand.

The Copyright Owners try to muddy the waters by claiming that, because the D.C. Circuit did not overturn a different part of the Majority's determination—the Majority's mixing and matching of inputs and outputs from different experts' analyses to create its own model—it must have agreed the *Phonorecords II* rates were "too low." But the D.C. Circuit held only that the Majority had engaged in allowable "line-drawing and reasoned weighing of the evidence" in combining the Shapley analyses. *Id.* at 386. That is not a holding that the *Phonorecords II* rates are too low to satisfy the Section 801(b)(1) factors or that the settlement cannot serve as a benchmark.[4] Nor could it be, since the D.C. Circuit vacated the rate levels that resulted from the Majority's model. *See id.* at 381, 387.

2. The Copyright Owners' Other Arguments Are Unpersuasive

The Copyright Owners next assert (at 15) that the *Phonorecord II* rates are "too low" because payments to songwriters and music publishers are not "keep[ing] pace" with the popularity of streaming (as measured by the number of streams). But that implies that there should be a one-to-one relationship between increased streams and increases in mechanical royalty payments. *See* Copyright Owners' Br. at 15. That argument runs headlong into the Judges' unanimous rejection of the Copyright Owners' proposal for a per-stream mechanical royalty rate. In rejecting that rate structure, the Judges explained that the type of consumption-based payments the Copyright Owners argued for (and now argue for again) would interfere with beneficial price discrimination in the market: "Weighing all the evidence and based on the

[4] At most, the D.C. Circuit found that substantial evidence supported the Majority's finding as to the *first* 801(b)(1) factor. *See Johnson*, 969 F.3d at 388 (defining substantial evidence as "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion"). But that does not mean that the D.C. Circuit found that the *Phonorecords II* rates were "too low." Reaching such a conclusion requires balancing of *all four* statutory factors—three of which the court explicitly left open for this remand proceeding. *Id.* at 389.

reasoning in this Determination, the Judges conclude that a flexible, revenue-based rate structure is the most efficient means of facilitating beneficial price discrimination in the downstream market." *Phono III*, at 84 Fed. Reg. at 1934.

By contrast, the *Phonorecords II* rates are percentage-of-revenue based, which aligns incentives and means that mechanical royalties from streaming will grow as industry revenues grow. And that has occurred. The Services' accounting expert, Professor Mark Zmijewski, testified that streaming contributed directly to an increase in publisher revenues. Ex. 1070 ¶¶ 38, 40, 55, 81 (Zmijewski WRT); 4/12/17 Tr. 5783:2-12 (Zmijewski). In particular, he showed that royalties from streaming had increased dramatically for NMPA members in the years immediately preceding the *Phonorecords III* hearing, and that the increase in mechanical and performance royalties from streaming actually outstripped losses caused by the declining market for download sales. Ex. 1070 ¶¶ 38, 40, 55, 81 (Zmijewski WRT); 4/12/17 Tr. 5783:2-12 (Zmijewski); *see also Phono III*, 84 Fed. Reg. at 1986 (Dissent).

Faced with this, the Copyright Owners resort to deflection. They point out (at 15) that mechanical streaming payments by Amazon to Copyright Owners for its Prime Music service [redacted]. But, here, in addition to basing their complaint on a stream-based mechanical royalty rate that the Judges unanimously rejected, the Copyright Owners ignore that Prime Music specifically targets consumers with a lower willingness to pay. In other words, by offering a more limited catalog and more limited features than "full" services such as Amazon Music Unlimited, Prime Music created royalty-generating listeners who had not previously paid any money for streaming music. *See* Ex. 22 ¶ 3.17 (Hubbard WDT) (explaining that "Prime Music is different from other streaming services, targets a unique audience, [redacted]

[redacted],” and so “there are multiple channels through which Prime Music may garner additional royalties for copyright owners”); Ex. 132 ¶¶ 2.9-2.12, 2.18, 2.22 (Hubbard WRT) (explaining that Prime Music expanded Amazon’s music consumer base by appealing to consumers with a low willingness to pay for music, [redacted]); Ex. 249 ¶¶ 64-70 (Klein WRT) (explaining that [redacted]); 3/15/17 Tr. 1312:19-1315:15 (Mirchandani). Prime Music also [redacted], further benefiting the Copyright Owners. Ex. 111 ¶ 39 (Mirchandani WRT). This [redacted], does not in any way suggest that there is a problem with the *Phonorecords II* benchmark. To the contrary, it confirms that the system is working.[5]

Next, the Copyright Owners claim (at 16) that the *Phonorecords II* rates are “too low” because overall mechanical royalties declined during two very specific time periods—from 2013 to 2014 and from 2014 to 2015. But publishers’ own data shows that publishers’ royalties *increased overall* during those same periods. The publishers’ financials showed that publisher royalties were rapidly increasing overall, with streaming driving that increase. Ex. 1070 ¶¶ 38, 40 (Zmijewski WRT); 4/12/17 Tr. 5783:2-12 (Zmijewski); *see also* Katz WDRT ¶¶ 95-98 (showing that the increase in streaming has continued through 2020). Those increases in revenue have continued. According to the NMPA itself, “2019 was the fifth consecutive year of significant growth” in music publishing royalties “primarily because streaming continues to

[5] The Copyright Owners’ argument on this front is also incomplete, as they ignore that songwriters and publishers also receive substantial public performance royalties for the Services’ streaming.

grow at a fast pace."[6] And the health of the industry has resulted in recent investment in publishing catalogs (even after the D.C. Circuit's decision vacating the Final Determination), with some purchasers paying hundreds of millions of dollars for the rights to notable collections.[7]

Moreover, the Copyright Owners cannot blame streaming (at 16-17) for any decline in mechanical royalties. Bart Herbison, the head of the songwriters' own trade group, testified that he did not "blam[e] the loss of songwriters on streaming," because other factors, including piracy and "disaggregation of the album," had caused the decline in songwriter royalties to begin prior to the popularity of streaming. 3/23/17 Tr. 2937:6-13, 2940:9-2941:23, 2945:4-22, 2955:1-2956:19 (Herbison). Mr. Herbison also admitted that he was "not ascribing any large percentage of [lower mechanical royalties] to streaming." *Id.* And the empirical data discussed above, as synthesized by Professor Zmijewski, shows that streaming has led to an overall increase in publisher revenue. *See* Ex. 1070 ¶¶ 38, 40, 55, 81 (Zmijewski WRT); 4/12/17 Tr. 5783:2-12 (Zmijewski). Even more recent data demonstrates that the publishing industry has done extremely well in recent years.

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[6] *NMPA Honors Garth Brooks, Reports Over $3.7 Billion in 2019 Revenue*, NMPA, https://www.nmpa.org/nmpa-honors-garth-brooks-reports-over-3-7-billion-in-2019-revenue/ (last visited July 2, 2021).

[7] *See, e.g.*, Andy Greene, *Neil Young Sells Catalog Rights to Merck Mercuriadis' Hipgnosis*, Rolling Stone (Jan. 6, 2021), https://www.rollingstone.com/pro/news/neil-young-music-catalog-hipgnosis-investment-1110037/; Cathy Applefeld Olson, *Stevie Nicks Sells Majority Stake in Songwriting Catalog*, Forbes (Dec. 4, 2020), https://www.forbes.com/sites/cathyolson/2020/12/04/stevie-nicks-sells-majority-stake-in-songwriting-catalog/?sh=7762ba1f239a; Jem Aswad, *Red Hot Chili Peppers to Sell Song Catalog to Hipgnosis for Upwards of $140 Millions*, Variety (May 3, 2021), https://variety.com/2021/music/news/red-hot-chili-peppers-sell-catalog-hipgnosis-songs-1234965644/; Ben Sisario, *Bob Dylan Sells His Songwriting Catalog in Blockbuster Deal*, N.Y. Times (Dec. 7, 2020), https://www.nytimes.com/2020/12/07/arts/music/bob-dylan-universal-music.html.

Finally, the Copyright Owners say (at 17) the *Phonorecords II* rates are "too low" because declining mechanical royalties are purportedly making it "more difficult for songwriters to earn a living." That claim is at odds with both the empirical evidence discussed above and Mr. Herbison's admissions that streaming was not the cause of songwriters' woes. It also ignores that interactive streaming results in a second revenue stream for songwriters that amplifies the effect of the above-noted continued growth in musical works royalties for songwriters and publishers—public performance royalties received directly from the Services or from PROs. In any event, even if the Copyright Owners' argument were well-supported by the evidence, the argument only concerns the first Section 801(b)(1) factor. On remand, the Judges must consider the parties' proposals in light of *all four* Section 801(b)(1) factors. *See Johnson*, 969 F.3d at 389.

In short, the Copyright Owners' assertion that the *Phonorecords II* benchmark should be rejected because the rates are "too low" does not withstand scrutiny.

B. The Copyright Owners Fail To Prove that Differences in Market Conditions Impact the Suitability of the *Phonorecords II* Benchmark

The Copyright Owners' next argument—that market conditions have so changed since the time of the *Phonorecords II* settlement that it cannot serve as a benchmark (at 17-26)—resurrects an argument the Majority and Judge Strickler both rejected and misunderstands the economically relevant market conditions.

To start, the Copyright Owners' "market conditions" argument is not about the market characteristics of interactive streaming at all. The Copyright Owners make no effort to address the key economic features of that market, which is characterized by differences in consumers' willingness to pay to listen to music and a product with zero marginal physical costs. *See Phono III*, 84 Fed. Reg. at 1999 (Dissent). Those features also characterized the market at the time of the *Phonorecords II* settlement, and experts on both sides agreed those features continue to do so today. *E.g.*, 3/20/17 Tr. 1829:2-4, 1967:12-1968:1 (Marx); Ex. 1069 ¶¶ 115-16 & Fig. 9 (Marx WRT); 3/13/17 Tr. 558:1-9 (Katz); 3/15/17 Tr. 1122:18-1123:8 (Leonard); 4/3/17 Tr. 4428:6-4431:22 (Rysman); *see also* 4/4/17 Tr. 4843-44 (Eisenach); 4/3/17 Tr. 4390, 4431 (Rysman).

The Copyright Owners instead suggest (at 21-22) that differences in the entities operating streaming services is a relevant change in marketplace conditions. In their words: "[i]n the years following the *Phonorecords II* settlement and leading up to this proceeding, Spotify was joined in the U.S. interactive streaming market by some of the largest multidimensional companies in the world." Copyright Owners' Br. at 21. The problem with this argument, however, is that these large "multidimensional" companies—including Amazon, Apple, and Google—already offered Section 115 services at the time of *Phonorecords II* or were participants in the *Phonorecords II* proceeding and had made their intentions of offering a Section 115 service known. *See* Ex. 6014 (showing signatories to *Phonorecords II* settlement agreement); 3/29/17 Tr. 3761:7-3763:13 (Israelite) ("Yes, Amazon, Apple, Google, Pandora were all participants and members of DiMA, I believe."); 3/15/17 Tr. 1308:11-14 (Mirchandani); Trial Ex. 697 ¶ 6 (Levine WRT); Trial Ex. 692 ¶¶ 38-39 (Levine WDT) (Describing Google's involvement: "We negotiated over locker services, 'limited' offerings and various bundled offerings . . . ."). And Spotify, while not a participant, had already launched in the United States. 3/29/17 Tr. 3762:24-3763:13 (Israelite) (admitting that Spotify was already operating in the U.S. at time of *Phonorecords II*).

Further, the Copyright Owners' own expert on investment in the streaming industry, Jim Timmins, admitted that the same types of "major" and "multidimensional" businesses had already existed in the streaming industry for some time before *Phonorecords II*. 3/28/17 Tr.

3394:21-3395:15, 3397:22-3399:2 (Timmins); *see also* 3/29/17 Tr. 3838:9-3839:22 (Israelite); Trial Ex. 697 ¶ 6 (Levine WRT); 3/8/17 Tr. 155:14-157:12 (Levine). Specifically, Mr. Timmins explained that there have been sequential waves of investments in the streaming industry, including one in the mid-2000s, in which (then) major technology companies like AOL and Yahoo! launched streaming services. 3/28/17 Tr. 3396:24-3397:11 (Timmins). In fact, in *Phonorecords I*, the Copyright Owners raised the same arguments about "multi-dimensional" companies pursuing a variety of revenue models that they make now:

> Q. Let me ask you to take a look at page 27. Do you see where your expert states, "subscription-based services pursue a variety of revenue models. The principal objective of companies such as Yahoo is to attract users to its site in order to sell on-line advertising. Music subscription services are important elements in helping to drive users to web portals such as Yahoo and to that extent aggressively price their offerings in order to maximize subscriber numbers."
>
> That's a position that was articulated by the Copyright Owners back in 2006, correct?
>
> A. This appears to be from one of our expert's reports from 2006, yes.

3/29/17 Tr. 3835:4-17 (Israelite).

The Copyright Owners' claim (at 22) that "[n]one of these multi-dimensional companies had entered into the interactive streaming market until after both *Phonorecords I* and *II*" simply finds no support in the record. Even aside from that, the Copyright Owners offer no explanation as to why this asserted change in participants calls into question the validity of the *Phonorecords II* benchmark. Indeed, as Professor Katz explained, the presence of technology companies in the interactive streaming market has led to significant innovation and resulted in significantly higher royalty payments to Copyright Owners. Ex. 885 ¶¶ 95-96 (Katz WDT). That change, if anything, calls for lowering mechanical royalty rates, not raising them above the *Phonorecords II* levels, to fairly compensate the Services for their investments, risks, and contributions to the industry. *Id*.

The Copyright Owners next argue (at 20-21) that they could not have anticipated the popularity and growth of streaming at the time of the *Phonorecords II* agreement. Once again, the Copyright Owners fail to explain why, even if true, this contention would affect the validity of the *Phonorecords II* benchmark. The *Phonorecords II* settlement was designed to foster growth in the streaming industry and compensate the Copyright Owners for that growth. As noted, this growth in streaming has led to ever-increasing royalty payments to the Copyright Owners and has been the catalyst for revitalizing the music industry. How that translates into a need for increased percent-of-revenue rates is never explained. But, in any event, this contention is factually wrong. At the time of *Phonorecords II*, there were already more than 3.4 million paying subscribers to interactive streaming services in the U.S., with tremendous year-over-year growth occurring at the time of *Phonorecords II*. Ex. 6 at 1 (RIAA data). The participants in *Phonorecords II* knew that streaming was the future and that there was no going back. Ex. 697 ¶¶ 5-6 (Levine WRT); 3/8/17 Tr. 171:7-172:6, 270:8-272:19 (Levine); *see also* Services' Joint PFFF ¶¶ 128-139 (containing the Services' evidence of what information was available at the time). There were already pure-play services operating under the same business model as today's market participants that had been in operation for over a decade and had large numbers of paying subscribers in the U.S. by *Phonorecords II*. Ex. 697 ¶ 6 (Levine WRT) (discussing how Rhapsody had already amassed over one million subscribers). And multiple other streaming services with the same or similar business models entered the market before 2012, including Yahoo!, AOL, Rdio, MOG, Napster, Slacker, and Groove Music. 3/8/17 Tr. 155:14-157:12 (Levine). All of the facts suggest that growth in the industry was very much foreseeable.

That the industry grew even more after *Phonorecords II* and continues to grow today is a reason to retain the *Phonorecords II* rate levels and rate structure, not discard them. Indeed, because parties on both sides at the time of the settlement knew that streaming was becoming a significant way to listen to music, the *Phonorecords II* settlement was intentionally designed to accommodate the growth of streaming and address the concerns the Copyright Owners raise. To start, the rate structure pegged royalty payments to growth in Services' revenues and the number of subscribers. That structure also included multiple types of service categories and provided multiple layers of downside protection to Copyright Owners, including floor fees. These protections were already present in the *Phonorecords II* settlement precisely because the Copyright Owners knew that streaming was becoming a significant source of revenue and that large, diversified companies would operate streaming services, so they negotiated terms specifically to address the same supposed issues about revenue deferment they raise now. *Phono III*, 84 Fed. Reg. at 1932 (finding Copyright Owners proposed the *Phonorecords I* and *II* structure as a way to protect against revenue deferment issues). In fact, Mr. Israelite and other NMPA witnesses raised the same issue of market growth in *Phonorecords I*. S*ee* 3/29/17 Tr. 3839:14-3843:6; 3844:6-3845:2 (Israelite) (explaining that the NMPA negotiated for a multi-tiered rate structure as a result of "having foreseen what [Israelite] refer[s] to as the reality that has come to pass"; answering questions from Judge Strickler concerning how the NMPA incorporated protections against revenue deferment into the *Phonorecords I* settlement); Ex. 6021 (Israelite testimony from *Phonorecords I* discussing the importance of defining how the revenue base is calculated due to concerns over business models of new market entrants). This fact alone undercuts Copyright Owners' argument that the parties to the settlement could not have anticipated the growth of interactive streaming at the time of *Phonorecords II*.

In the end, the central question when assessing whether the *Phonorecords II* settlement is a good benchmark is whether there have been changes that call for adjustments to the rate levels or rate structure of that benchmark. The Services and their experts have done that analysis and have demonstrated that the changes that have occurred in no way call for any upward adjustment to the *Phonorecords II* rates. Services' Br. at 24-34. If anything, the changes that have occurred call for lowering the rates, as the Copyright Owners have done exceptionally well under that settlement, earning ever-increasing royalties, while the Services continue to lose money. *See Phono III*, 84 Fed. Reg. at 1999 (Dissent) ("[T]he parties have been operating over the past ten years under this basic rate structure, with profits accruing to the licensors and admittedly tolerable losses for the licensees."). Simply pointing out things that have allegedly changed, without providing any supporting rationale for why those changes warrant a departure from what has proven to work well for the Copyright Owners for a decade, in no way undermines the Services' showing.

C. Evidence of Subjective Intent Is Not Required To Adopt a Benchmark

The Copyright Owners argue that the Services had a burden of presenting evidence of the subjective intent of the parties to the *Phonorecords II* settlement, and that the Services did not meet that burden. Copyright Owners' Br. at 4, 27-31. The Copyright Owners further suggest (but do not actually attempt to prove) that other factors—primarily the NMPA's economic constraints—may have prevented adequate negotiation of the *Phonorecords II* settlement. *Id*. at 30-31. These arguments are wrong as a matter of law and are at odds with the factual record.

1. There Is No Burden To Present Evidence of Subjective Intent

There is no burden to present evidence of the negotiating parties' subjective intent in support of a benchmark. As the Majority correctly noted, "[r]elying on a benchmark as *objectively* useful without [the need for] further inspection" is "typical and appropriate for the benchmarking method." *Phono III*, 84 Fed. Reg. at 1944 & n.106 (emphasis added). Judge Strickler agreed, noting that "the absence of more direct testimony regarding what went through the minds of the negotiators of the 2008 and the 2012 settlements does not diminish the *objective* value of this [*Phonorecords II*] benchmark." *Id*. at 2000 (Dissent) (emphasis added).

The Copyright Owners cite *Intercollegiate Broadcast System* to support their argument, suggesting that the decision in that case holds that evidence of subjective intent is required to support a benchmark. It holds nothing of the sort. There, the Board rejected a benchmark containing a lump-sum payment because the proponent of the benchmark did not provide adequate evidence to demonstrate how the lump sum could be used to derive a useful per-year or per-station royalty rate for the services at issue. *Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd.*, 574 F.3d 748, 764-65 (D.C. Cir. 2009) (per curiam). In other words, the Board rejected the benchmark in that case because the four corners of the agreement did not provide the Judges with enough evidence for it to be a useful *objective* benchmark—a problem that neither the Majority nor Judge Strickler had with the *Phonorecords II* benchmark. The Copyright Owners also suggest (at 27) that the Majority agreed with the proposition that evidence of subjective intent is necessary to support a benchmark. That too is wrong. The portion of the Majority opinion that the Copyright Owners cite (84 Fed. Reg. at 1944 & n.106) simply notes that the Copyright Owners raised this criticism and then goes on to explain that relying on a benchmark as objectively useful is "typical and appropriate for the benchmarking method." *Id*. It comes to the exact opposite conclusion that the Copyright Owners do. There is no support in the Final Determination for the Copyright Owners' argument.

2. The Record Contains Evidence Concerning the Negotiations

While evidence of subjective intent is not required to credit a benchmark, the Services provided ample evidence about the *Phonorecords II* negotiations through the testimony of two separate witnesses. The Copyright Owners argue that those two witnesses, Adam Parness and Zahavah Levine, were not personally present in negotiation meetings with the NMPA in 2008 and 2012. *See* Copyright Owners' Br. at 27 n.9. However, the record is clear that both Mr. Parness and Ms. Levine were "involved in the contemporaneous internal discussions of negotiation strategy on behalf of the Services." *Phono III*, 84 Fed. Reg. at 1989 (Dissent) (noting the involvement of Mr. Parness and Ms. Levine in negotiations through DiMA, the trade organization representing digital licensees in *Phonorecords I* and *II*). Indeed, both the Majority and Judge Strickler cited the testimony of Ms. Levine and Mr. Parness concerning aspects of the negotiations. *See, e.g.*, *id*. at 1928, 1932, 1989, 1994, 2014.

Ms. Levine and Mr. Parness provided testimony regarding the circumstances under which the benchmark was negotiated, including market conditions at the time, the bargaining positions of each party (including specific changes the NMPA requested between *Phonorecords I* and *II*), which side proposed different aspects of the rate structure, the Services' expectations and reasons for agreeing to the rate structure, what was known about the future of the industry at the time of negotiations, and how the parties reached a compromise. *See, e.g.*, Services' Joint PFF ¶¶ 122-31; Services' Responses to Copyright Owners' COF 421-22 and 426-30; Ex. 692 ¶¶ 37-41 (Levine WDT); Ex. 875 ¶¶ 4-14 (Parness WDT); Ex. 697 ¶¶ 2-6 (Levine WRT). The Copyright Owners' suggestion that this uncontroverted evidence is insufficient demonstrates the absurdity of the evidentiary standard they are advocating. It would be impossible for any participant to adduce evidence as to every intention of every party to an agreement, whether expressed or not—particularly an industrywide agreement like the *Phonorecords II* settlement. Indeed, as the Majority noted, the Copyright Owners themselves did not even attempt to meet this burden when putting forward their own benchmark agreements. *Phono III*, 84 Fed. Reg. at 1944 & n.106.

3. The Copyright Owners Fail To Present Any Evidence that the **Phonorecords II** *Settlement Was Driven by Other Circumstances*

The Copyright Owners contend that evidence of subjective intent "would have revealed whether the agreed-upon rates were based on economic realities or instead were driven by other considerations." Copyright Owners' Br. at 30-31.[8] If the Copyright Owners truly thought evidence of the subjective intent of the negotiating parties would undermine the utility of the *Phonorecords II* settlement as a benchmark, it was their burden to come forward with such evidence during the hearing. Complaining about a lack of evidence now or, worse, speculating about what that evidence *might* have shown is insufficient. *See Determination of Royalty Rates and Terms for Ephemeral Recording and Webcasting Digital Performance of Sound Recordings* (*Web IV*), Final Rule, 81 Fed. Reg. 26316, 26384-85 (May 2, 2016) (finding that a party alleging "additional value" not reflected in a benchmark must provide an "evidentiary basis to support" the challenge).

In fact, the Copyright Owners previously tried—and failed—to present evidence that "other considerations" drove the *Phonorecords II* settlement. At trial, Mr. Israelite testified that the financial condition of NMPA members led the NMPA to quickly enter into an agreement without adequate negotiations. But, beyond the say-so of Mr. Israelite, the Copyright Owners presented no evidence regarding the NMPA members' financial position in 2011-2012 or how that impacted the NMPA's negotiation strategy. And Mr. Israelite's testimony on the matter proved to be unreliable. Specifically, the Services established that the NMPA engaged in a lengthy, year-long negotiation with the Services that included, *inter alia*, negotiations over rate

[8] The Copyright Owners suggest further (at 30-31) that the D.C. Circuit blessed this view, but again the D.C. Circuit's opinion says no such thing. It merely notes that the Copyright Owners advanced this argument on appeal. *See Johnson*, 969 F.3d at 387 (making clear that the court was quoting the Copyright Owners' brief).

levels, creation of new service categories, and changes to how the TCC prong was calculated. 3/8/17 Tr. 159:1-24, 161:2-164:11 (Levine); 3/29/17 Tr. 3856:2-6 (Israelite). In the Final Determination, neither the Majority nor Judge Strickler credited Mr. Israelite's testimony as a basis for rejecting the benchmark. S*ee, e.g.*, *Phono III*, 84 Fed. Reg. at 1988 (Dissent); *see also id*. at 1932 (Majority) (noting that the rates "were the subject of negotiation" and not mentioning Israelite's claim that NMPA simply rolled over existing rates). This perhaps explains why the Copyright Owners now have pivoted to arguing for a non-existent legal standard—that the Services must prove a negative (*i.e.*, that there is no evidence of intent outside the record that would undermine the objective value of the *Phonorecords II* benchmark).

D. The Copyright Owners' "Other Reasons" for Opposing the Benchmark Also Fail

The Copyright Owners resort to re-litigating several issues that have already been decided against them. They argue that the settlement is infected by the "shadow of the rate court," that it is improper to use a settlement as a benchmark, and that the "de novo" clause in the settlement prevents it from being considered as a benchmark. These are merely variations (or restatements) of arguments that the Judges have already rejected or ignored, and the Copyright Owners have offered no basis for why it is appropriate to reconsider these issues now.

1. The "Shadow of the Rate Court" Does Not Negate the **Phonorecords II** *Settlement as a Benchmark*

The Copyright Owners' argument that the Judges cannot employ a benchmark influenced by the "shadow of the rate court" is without merit. To start, the Judges already rejected this argument in this proceeding and others. *Phono III*, 84 Fed. Reg. at 1932-33; *see also Web IV*, 81 Fed. Reg. at 26331 ("[T]he Judges emphasize that they find the 'shadow' criticism to be both nihilistic and self-contradictory. If the 'shadow' infects all benchmarks so as to disqualify that method of rate-setting, then the parties would need to adjust or abandon their benchmarking strategies and develop new bases for analysis.").

In addition, there is no legal basis to reject a deal as a benchmark solely because it was negotiated against the backdrop of a statutory license. As the Judges recognized, Section 115 expressly authorizes consideration of direct deals, including settlements struck by entities subject to the statutory licenses the Judges oversee. *Phono III*, 84 Fed. Reg. at 1932-33 (noting that Section 115 provides that "in establishing such rates and terms, the Copyright Royalty Judges may consider rates and terms under voluntary license agreements described in subparagraphs (B) and (C)"). The Copyright Owners' argument suggests that no benchmarks could ever come from the regulated market, which cannot be squared with the Judges' explicit authorization to consider direct agreements.

Finally, the Copyright Owners have failed to present evidence that the "shadow of the rate court" makes the *Phonorecords II* settlement an inferior benchmark when compared to available alternatives. As the Majority recognized, "there is no reason to find such benchmark agreements per se inferior to other marketplace benchmark agreements that may be unaffected by the shadow, because the latter may be subject to their own imperfections and incompatibilities with the target market." *Phono III*, 84 Fed. Reg. at 1933. And, in this case, the Services have shown that the influence of the "shadow" makes the *Phonorecords II* benchmark more informative of reasonable rates. As Professor Katz explained, the existence of the statutory license prevents the Copyright Owners from obtaining unduly high rates by using their oligopoly power over mechanical rights to threaten to "walk away" and withhold their catalogues entirely. *Id*. at 1933; *see also id*. at 1993 (Dissent) (noting in response to the "shadow" argument that "such settlement agreements tend to eliminate complementary oligopoly inefficiencies, and provide guidance as to an effectively competitive rate.").

2. There Is No Prohibition on Using Settlements as Benchmarks

The Copyright Owners briefly argue that all settlements are *per se* bad benchmarks because adopting a settlement as a benchmark will "chill future settlements" and because such benchmarks are influenced by the "trade-offs motivated by avoiding litigation cost." Copyright Owners' Br. at 35. Copyright Owners have no support for this position other than the unqualified opinion of Mr. Israelite, *see id*., which stands in contrast to the regular practice of rate courts. Indeed, rate-setting tribunals, including this one, often rely on settlements when engaging in benchmark analysis. *See, e.g.*, *Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services* (*SDARS II*), Final Rule, 78 Fed. Reg. 23,054, 23,084 (April 17, 2013) (crediting PSS rates settled in *SDARS I* as a starting place for Section 801(b)(1) analysis); *In re Application of MobiTV, Inc*., 712 F. Supp. 2d 206, 222 (S.D.N.Y. 2010) (relying on past ASCAP settlements as benchmarks; the court referred to the settlements as the "Post-*Turner* Licenses" because they were arrived at through settlement "after lengthy litigation known as the *Turner* litigation"); *see also* Review of Copyright Royalty Judges' Determination, 78 Fed. Reg. 22,913, 22,915 n.9 (Apr. 17, 2013) (declining to find error based on use of past settlement of statutory license as a benchmark, though the argument was raised by the parties).

Moreover, the Copyright Owners' argument against considering settlements as benchmarks—like their argument concerning the "shadow of the rate court"—is in conflict with the Copyright Act. As noted above, Section 115 expressly allows the Board to consider voluntary agreements that settle rate-setting proceedings. *See Phono III*, 84 Fed. Reg. at 1932-33 (concerning the Judges' ability to rely on voluntary agreements); *id*. at 1999 (Dissent) ("I re-emphasize that, as a matter of law, section 115 specifically provides that settlements shall constitute evidence of market rates.”). Further, all voluntary licenses pertaining to rights governed by a statutory license could be characterized as “settlements” that avoid the need for rate-setting litigation. Taken to its logical end, a prohibition on using settlements as benchmarks would prevent using all direct agreements from the relevant market as benchmarks, which would deprive the Judges and parties of well-established tools used in rate-setting analysis. *Cf. Web IV*, 81 Fed. Reg. at 26,331 (noting that a participant’s argument against relying on benchmarks from the “shadow” of the rate court was “nihilistic” and flawed because it could lead to the “wholesale abandonment of benchmarking”).

To be sure, some settlements are better benchmarks than others. For instance, an industry-wide settlement of a rate proceeding, like the *Phonorecords II* settlement, is a particularly useful benchmark because of its scope, the fact that it reflects the judgment of multiple market participants rather than the economic considerations or trade-offs faced by a single participant, and the fact that the rights in question are identical to those at issue in the rate proceeding in which the settlement is offered as a benchmark. *See* Katz WDT ¶¶ 68-71; *see also Phono III*, 84 Fed. Reg. at 1993 (Dissent) (discussing benefits of industry-wide settlements as benchmarks). And while the Copyright Owners attack the use of settlements on a categorical level, they have failed to present credible evidence proving that the rates in *this* settlement were the product of noneconomic factors or were otherwise infected by outside influences that make the benchmark unreliable. *See Web IV*, 81 Fed. Reg. 26,384-85 (rejecting a benchmark challenge due to party’s failure to develop an evidentiary basis for its challenge); *see also id*. at 26,330 (rejecting a benchmark challenge and noting that, “[i]f a benchmark is deficient in some manner, the adversarial process of this proceeding allows the parties to expose those deficiencies"). Indeed, the Copyright Owners have not established that non-economic factors, such as the cost of litigating the *Phonorecords II* rates, outweighed the potential gains available to the Copyright Owners through litigation, or that considerations surrounding the cost of litigation were more significant for the Copyright Owners than they were for the Services. Nor could they. Given that the mechanical royalties for the entire interactive streaming industry over a five-year period were at issue in *Phonorecords II*, it is not plausible that litigation costs would have materially affected the terms of the settlement, as such costs would have been swamped by the amount of royalties at issue. Copyright Owners lack evidence to support any notion that the *Phonorecords II* benchmark is flawed simply because it arose from a settlement.

3. The "De Novo" Language in the **Phonorecords II** ***Settlement Does Not Bar Its Use as a Benchmark***

The Copyright Owners make much of the fact that the *Phonorecords II* settlement suggested that future rates should be set "de novo." Copyright Owners' Br. at 26. But the cited "de novo" language does not mean that the settlement cannot be used as a benchmark; it simply means the rates contained in the *Phonorecords II* regulations were not set forever and that, in future proceedings, the Judges would reevaluate the Section 801(b)(1) factors on the record presented. As Judge Strickler explained, "[i]n the *Phonorecords II* settlement, the parties agreed that any future rate determination for subparts B and C configurations presented to the Judges would be a *de novo* rate determination. However, they did not agree that the existing rate structure or rates could not be considered as the bases for future rate determinations." *Phono III*, 84 Fed. Reg. at 1970 n.187 (Dissent) (citation omitted).

The Copyright Owners' position that "de novo" means that the settlement is barred from consideration as a benchmark is also belied by the negotiation history. As the record demonstrated (and as Judge Strickler noted), the parties in *Phonorecords I* agreed that the royalty rates in that settlement "shall not be cited, relied upon, or proffered as evidence or otherwise used in the Proceeding." *Id.*; Ex. 6013. Yet the *Phonorecords II* settlement contained no such limitation. *Phono III*, 84 Fed. Reg. at 1970 n.187 (Dissent); Ex. 6014. In other words, the parties understood the precedential implications of settlements and knew how to include non-precedential language when intended, yet they chose not to do so in the *Phonorecords II* settlement. *Id.*[9]

III. THE VACATED RATE STRUCTURE AND RATE LEVELS DO NOT SATISFY THE RATE-SETTING STANDARD AND THE COPYRIGHT OWNERS HAVE OFFERED NO CREDIBLE BASIS FOR REINSTATING THEM

Instead of attempting to meet their burden of showing that the vacated rate levels and rate structure are reasonable and satisfy the Section 801(b)(1) factors, the Copyright Owners ask the Judges (at 37) to simply reinstate the rate levels and structure based on the "same . . . reasoning" in the Final Determination. The Copyright Owners argue (at 55) that this result is warranted because the Services purportedly cannot demonstrate that an uncapped TCC prong for subscription interactive services will "directly produce[ ] an adverse impact that is substantial, immediate and irreversible in the short-run." Not so. The Judges' charge in this remand proceeding is to determine rate levels and a rate structure that are reasonable and satisfy all of the Section 801(b)(1) factors. Nothing in the Judges' mandate or the *Johnson* decision suggests it would be appropriate to assess only whether the Final Determination caused "substantial" "short-

[9] In footnote 16 of their opening brief, the Copyright Owners concoct a reason why the non-precedential language of the *Phonorecords I* settlement was not included in the *Phonorecords II* settlement, yet they fail to support the explanation with any record evidence. *See* Copyright Owners' Br. at 34 n.16 (citing only to the Copyright Owners' own proposed findings, which do not contain evidence to support the Copyright Owners' new narrative concerning the elimination of the non-precedential clause). Yet, even if the Copyright Owners' explanation were correct, it remains inapposite. The point stands that no language in the *Phonorecords II* settlement bars its introduction as a benchmark in future proceedings.

run" disruption, and "reinstate" the vacated rate levels and rate structure it if it did not. The Judges should reject the Copyright Owners' invitation to supplant the governing rate-setting standard with their own invented standard.

The Copyright Owners' effort to manipulate the legal framework only underscores how little they have to say about the *actual* question before the Judges—whether their proposal to reinstate the vacated rate levels and rate structure is reasonable and satisfies all four Section 801(b)(1) factors. Perhaps most notably, the Copyright Owners offer virtually no defense of the see-saw theory: the "heroic assumption" that was central to the Majority's reasoning in adopting both the now-vacated rate levels and rate structure. *Phono III*, 84 Fed. Reg. at 1966 (Dissent); *Phono III*, 84 Fed. Reg. at 1953; *see also* Services' Br. at 44-50. And what little effort the Copyright Owners do make to defend the see-saw theory falls short, especially given all of the evidence demonstrating that the theory is based on a flawed model and has not manifested itself in reality. Services' Br. at 47-50. Recognizing that the predictions of the see-saw theory have not come to pass, the Copyright Owners did not introduce any new evidence in support of that theory in their opening remand submission.

The Copyright Owners likewise offer no serious defense of the vacated rate levels. They make no effort to demonstrate that those rates are reasonable and satisfy the four Section 801(b)(1) factors, despite the fact that the D.C. Circuit explicitly left that issue open for this remand proceeding. *Johnson*, 969 F.3d at 384, 388-89.

With respect to the rate structure, the Copyright Owners only offer a single argument: that an uncapped TCC prong for subscription interactive services is necessary to protect the Copyright Owners against revenue deferment and displacement. That argument is not only wrong, but also ignores the significant substantive concerns with the vacated rate structure that the D.C. Circuit raised: whether a rate structure that "yokes the mechanical license royalties to the sound recording rightsholders' unchecked market power" could be reasonable and satisfy all of the Section 801(b)(1) factors. *Id*. at 382-83.

Finally, the Copyright Owners devote numerous pages to re-litigating arguments that the Judges have already rejected and that, in any event, are irrelevant to this remand proceeding. The Copyright Owners' efforts at misdirection should be seen for what they are and should be rejected once again.

The vacated rate levels and rate structure should not be reinstated.

A. The Copyright Owners' Singular Focus on the Disruptive Impact of the Uncapped TCC Prong Is Misplaced

Unable to marshal facts to support reinstatement of the vacated rate levels and rate structure, the Copyright Owners try to manipulate the legal framework. Copyright Owners' Br. at 7, 47-48, 55-56. The Copyright Owners argue that the Services have the burden of proving that an uncapped TCC prong for subscription interactive services is disruptive and, if the Services cannot meet that invented burden, the vacated rate structure (and the vacated rate levels) should be reinstated. *See, e.g.*, Copyright Owners' Br. at 55-56.

The Copyright Owners' argument makes no sense. Whether the uncapped TCC prong for subscription interactive services is disruptive is but *one* of the factors that must be considered when assessing whether the vacated rate structure and rate levels should be reinstated. The task before the Judges is to determine rate levels and a rate structure that are reasonable and satisfy *all four* Section 801(b)(1) factors. *See Johnson*, 969 F.3d at 368-69. And, as the Services have demonstrated, the central justification for the prior determination—the see-saw theory—is fundamentally flawed as a theoretical matter and has now been disproved as an empirical matter. Services' Br. at 44-50. Under such circumstances, the Judges cannot reinstate the same flawed determination based on the "same . . . reasoning" because the Services have purportedly failed to prove that the "adverse impacts" of the uncapped TCC prong have been "so substantial that they 'threaten the viability'" of the Services. Copyright Owners' Br. at 37, 56.

Moreover, the Services do not have any burden of proving that an uncapped TCC prong for subscription interactive services is disruptive, let alone that it is so disruptive that it threatens their viability. The Services instead need to demonstrate that their proposal is reasonable and satisfies the four Section 801(b)(1) factors—the same burden that the Copyright Owners have with respect to their proposal. The Services not only have met that burden as to their proposal, Services' Br. at 19-43, but also have demonstrated, including with new evidence, that the vacated rate levels and rate structure that the Copyright Owners propose are *not* reasonable and do *not* satisfy the Section 801(b)(1) factors. Services' Br. at 44-64.

The Copyright Owners, on the other hand, have made no effort to support their preferred rate levels—despite the fact that the D.C. Circuit vacated those rate levels and expressed significant concerns with them. *See supra* Section I. The Copyright Owners do not even *mention* the second and third Section 801(b)(1) factors in their opening submission, let alone attempt to explain how the vacated rate levels satisfy those factors, even though the D.C. Circuit left open that question for the remand proceeding. *See id.* The Copyright Owners' silence as to these central issues speaks volumes.

As to the single issue the Copyright Owners attempt to make this remand proceeding all about—whether an uncapped TCC prong for subscription interactive services satisfies the fourth Section 801(b)(1) factor—the Copyright Owners are wrong there too. To start, the full extent of the disruption to the Services from an uncapped TCC prong was never tested in the marketplace. The Majority set escalating rates, and the Final Determination was vacated before the "significant[] hike[]" in rate levels was fully implemented. *Johnson*, 969 F.3d at 382-83. Put simply, there was never a chance to evaluate the full extent of the ruling's disruptive impact. As a result, the Copyright Owners' attempt to make this entire remand proceeding about the observed disruptive impact before the D.C. Circuit vacated the Final Determination is misguided. Further, as demonstrated in the Services' opening submission, even during the limited period when the TCC cap was removed, [redacted]. Services' Br. at 58-60; Mirchandani WDRT ¶¶ 10-11; *see also* Ex. C, Marx Remand Dep. Tr. 20:2-8 ([redacted]).

In the end, no determination on remand could withstand appellate scrutiny without addressing the entirety of the rate-setting standard as to both rate levels and rate structure. The Services have done that. The Copyright Owners, on the other hand, have not.

B. The Copyright Owners' Effort To Salvage the "See-Saw" Theory Fails

As explained in the Services' opening brief (at 44-50), the vacated rate levels and rate structure rested upon a faulty premise—the flawed see-saw theory that has since been debunked by several years of real-world experience. The Copyright Owners do not even try to introduce new evidence in support of this theory, and their defense of the theory based on the existing record is without merit.

First, the Copyright Owners now disclaim the only witness testimony that the Majority cited to support the see-saw theory. Specifically, having been confronted with the many flaws in the model Professor Watt prepared to support the see-saw theory and the fact that the see-saw theory has not materialized in the real world, the Copyright Owners now take the position that Professor "Watt's report as a whole makes clear that his Nash bargaining analysis was *never a* *guarantee of any particular outcome*." Copyright Owners' Motion to Compel, at 8 (emphasis added). But Professor Watt's assertion, based on his Nash bargaining model, that sound recording royalties would come down to almost entirely offset any increase in musical works royalties was central to the Majority's findings on rate levels and rate structure. *See, e.g.*, *Phono III*, 84 Fed. Reg. at 1953 ("[T]he Judges rely on Professor Watt's insight (demonstrated by his bargaining model) that sound recording royalty rates in the unregulated market will decline in response to an increase in the compulsory license rate for musical works."); Services' Br. at 44-50. That the Copyright Owners made this admission—that the model providing the *sole support* for the see-saw theory cannot be relied upon to predict how sound recording rates will actually respond to changes in mechanical rates—should put a quick end to the notion that the see-saw theory is valid.

Despite their concession, the Copyright Owners nevertheless attempt to defend the see-saw theory (at 66-67) on grounds the Majority never invoked. In particular, the Copyright Owners point to [redacted] as empirical support for the theory. But none of these agreements supports the notion that record labels would voluntarily "accept millions of dollars in lost revenue" from interactive streaming services by agreeing to "lower sound recording royalties" in response to an increase in mechanical rates. *Phono III*, 84 Fed. Reg. at 1966 (Dissent). [redacted].

[redacted].

Copyright Owners' Br. at 67. [redacted]

[redacted]. By pointing only to isolated agreements without examining how sound recording rates have (or have not) actually changed in response to changes in musical works rates, the Copyright Owners offer nothing of relevance.

The single [redacted] agreement that the Copyright Owners point to similarly fails to address whether a see-saw effect will ever take place and, if anything, only further undermines the see-saw theory. As the Copyright Owners note (at 67), [redacted].[10] Dissent at 116, *Phono III*, No. 16-CRB-0003-PR (2018-2022) (Nov. 5, 2018) (Dissent). [redacted]. Such a result is directly at odds with the see-saw theory. And, as with the PDD agreements, because the Copyright Owners only cite a single agreement at one point in time, the [redacted] agreement offers no insight into how record label fee demands *change* in response to changes in musical works rates.

In addition to pointing to these uninformative agreements, the Copyright Owners also attempt to recast expert testimony discussing the theoretical possibility of a see-saw effect (at 65-66) as somehow proving that Professor Watt's see-saw prediction will occur. Judge Strickler already addressed this argument and concluded that the testimony the Copyright Owners cite is

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[10] [redacted] Dissent at 18.

"indeterminate" and does nothing to move the see-saw theory out of the realm of a "hypothetically plausible idea." *Phono III*, 84 Fed. Reg. at 2027-28 (Dissent). And with the benefit of the experience of the last three years, we now know based on real-world data just how wrong the see-saw theory and Professor Watt's prediction were—there is no need to turn to "indeterminate" economic theory. In the time since the Initial Determination issued, [redacted]. Services' Br. at 14-16, 48-49 (collecting fact witness testimony); *see also* Ex. C, Marx Remand Dep. Tr. 149:2-17 ([redacted] (emphasis added)). The Copyright Owners, for their part, have offered no evidence that undermines this showing.[11]

What is more, on remand, Professor Marx, Professor Katz, and Dr. Leonard had the opportunity—for the first time—to analyze and address Professor Watt's model, which was introduced in rebuttal. They *all* agreed that it cannot be used to make any sort of reliable

[11] The Copyright Owners could, for example, have attempted to show some relationship between musical works royalties and sound recording royalties—information that Copyright Owner members have at their disposal, as it is included in their royalty statements from the Services. That the Copyright Owners chose to adduce no new evidence whatsoever on this issue (or any other) only underscores that Copyright Owners have no credible support for the see-saw theory.

prediction of how record label rates will change in the real world in response to changes in musical works rates. *See* Services' Br. at 49-50 (collecting expert witness testimony); *see also* Ex. C, Marx Remand Dep. Tr. 90:25-91:13 ([redacted]); Ex. A, Katz Remand Dep. Tr. 161:5-162:8 ([redacted]). This expert testimony provides yet another basis for rejecting Professor's Watt's prediction.

In addition, because [redacted]. We are now most of the way through the *Phonorecords III* license period, so [redacted]

[redacted]—an absurd proposition for which there is no evidence in the record. *See, e.g.*, Ex. A, Katz Remand Dep. Tr. 141:18-143:2 ([redacted]). Indeed, in several instances, [redacted] *See, e.g.*, White WDRT ¶ 19 ([redacted]).

Finally, the Copyright Owners pivot and argue (at 67-68) that the see-saw theory is effectively irrelevant because the Services failed to put in evidence demonstrating precisely how bad things need to get before each Service reaches its respective "shut down" point. The Copyright Owners seem to believe that, so long as the Services' total royalty obligations are not "unsustainable" in the short term, it is appropriate to keep increasing their musical works royalty obligations. *Id*. The Copyright Owners' evident belief that the Services should be forced to pay ever-increasing royalties up until they reach their "shut down" point exposes the Copyright Owners' deep misunderstanding of the purpose of this proceeding, which is to set *reasonable* rates that meet *all four* Section 801(b)(1) factors.[12] Among other things, these factors call for rates that ensure that both the Copyright Owners *and* the Services receive fair returns and appropriately reflect their respective contributions to the marketplace. The Copyright Owners' apparent understanding of the governing rate-setting standard is entirely at odds with these statutory directives.

C. The Copyright Owners' Sole Effort To Justify the Vacated Rate Structure Is Meritless

The Copyright Owners offer no serious defense of the vacated rate structure. They make only a single argument in support of it: that an uncapped TCC prong for subscription interactive services is necessary to protect against the possibility of revenue deferment or displacement by the Services in a revenue-based rate structure. Copyright Owners' Br. at 38-46. The Copyright Owners are wrong. Indeed, in their reply proposed findings, the Copyright Owners had expressed a very different view, arguing that an uncapped TCC prong "does nothing to protect Copyright Owners from the Services' revenue displacement and deferment." Copyright Owners' Reply to Google PFF & COL at 2; *see also Phono III*, 84 Fed. Reg. at 1964-65 (Dissent). The Copyright Owners have not even tried to explain away their complete about-face on this issue.

Moreover, the Services here are proposing a multi-pronged structure, with a headline percentage-of-revenue rate *and* a variety of other prongs, including minima and floors that

[12] The Copyright Owners also misunderstand the fourth Section 801(b)(1) factor. For a rate to be disruptive, it does not have to threaten the short-term viability of the Services, as the Copyright Owners claim. While that certainly would be disruptive, the Judges, in prior proceedings, have used the fourth Section 801(b)(1) factor to lower rates "in order not to significantly delay the attainment and amounts of EBITDA profitability and positive free cash flow." *Determination of Rates and Terms for Preexisting Subscription Services and Satellite Digital Audio Radio Services* (*SDARS I*), 73 Fed. Reg. 4080, 4097 (Jan. 24, 2008); *see also SDARS II*, 78 Fed. Reg. at 23,054, 23,069 (noting that the disruption factor calls for a downward adjustment to rates when the service was not sufficiently profitable).

protect the Copyright Owners from the very concerns they now raise. As Judge Strickler recognized, a multi-faceted rate structure with a capped TCC prong addresses the potential for revenue displacement or deferment and should be continued here. *Phono III*, 84 Fed. Reg. at 1990 (Dissent) ("[A] way in which the input supplier can mitigate the effect of such revenue deferrals is to establish a pricing structure that provides alternate rate prongs and floors, below which the royalty revenue cannot fall. This is precisely the bargain struck between the Copyright Owners and the Services in 2008 and 2012, and that has been ongoing through the present day."). The Copyright Owners do not take on Judge Strickler's reasoning.

Indeed, the structure adopted in *Phonorecords I* and *II*, which featured a capped TCC prong for subscription interactive services, was proposed by the *Copyright Owners* to address revenue deferment and displacement issues. *Phono III*, 84 Fed. Reg. at 1932 ("[Copyright Owners] claim to have accepted the present rate structure because it offered protection against poorly monetized services, through the establishment of the alternate prongs. In fact, it was Copyright Owners that first proposed the three tiered rate structure that now exists."). Similarly, the *Copyright Owners* insisted on "floor fees" as a means of protecting against unforeseen reductions in the mechanical rate. *Id*. Here, the Services' proposal retains both the capped TCC protection and floor fees, and the Copyright Owners have failed to demonstrate that those protections are now insufficient to address their concerns about revenue deferment and displacement.

In addition, the Copyright Owners fail to address the fundamental problem that the D.C. Circuit identified with imposing an uncapped TCC prong on subscription interactive services—that it "yokes" the mechanical license royalties the Services must pay to sound recording rightsholders' unchecked market power. *Johnson*, 969 F.3d at 382.[13] The Copyright Owners cannot explain why it makes any sense to adopt a one-sided rate structure that (they claim) protects them from revenue deferral and displacement concerns but, at the same time, exposes subscription interactive services to the sound recording rightsholders' unchecked market power. This sort of "greater-of" rate structure that "favor[s] one side of the transaction over the other" "do[es] not meet the standard of reasonableness." *Phono III*, 84 Fed. Reg. at 1984-85 (Dissent); *see also Web IV*, 81 Fed. Reg. at 26,323-26 (rejecting a similarly one-sided greater-of rate structure). Moreover, there is a tried-and-true approach for balancing these competing concerns that has worked well for a decade and to which the Copyright Owners agreed *twice*: adopting the Services' Proposal. Doing so protects the Copyright Owners from revenue deferral and displacement concerns and, at the same time, protects the Services from the unchecked market power of the sound recording copyright holders.

D. The Copyright Owners' Additional Arguments Are Irrelevant and Have Already Been Rejected by the Judges

The Copyright Owners' remaining arguments re-litigate settled issues that have no bearing on this remand proceeding. First, the Copyright Owners again assert that the Services had the opportunity to rebut Google's post-hearing proposal. The relevance of this is never explained, but in any event, the Copyright Owners are incorrect. Next, the Copyright Owners attempt to re-litigate whether the major record labels have market power, even though the Majority, Judge Strickler, and the D.C. Circuit have all acknowledged that the major labels have complementary oligopoly power over the Services. Finally, despite the D.C. Circuit's

[13] The Copyright Owners make the frivolous argument that sound recording rightsholders do not have any market power over subscription interactive services. That argument is dispensed with below. *See infra* III.D.2.

conclusions to the contrary, the Copyright Owners once again assert that an uncapped TCC prong must be reasonable for subscription interactive services because the Services proposed uncapped TCC prongs for other less-consequential products. Each of these arguments is without merit and, in any case, is irrelevant.

1. The Copyright Owners' Assessment of Google's Post-Hearing Proposal Was Rejected by the D.C. Circuit and Is Irrelevant

The Copyright Owners' argument (at 37) that the Services already had the opportunity to rebut Google's post-hearing fee proposal is plainly incorrect. The D.C. Circuit evaluated—and rejected—this very assertion in *Johnson*, finding that "Google's package was proposed for the very first time after the evidentiary record was closed. So the other parties never had a chance to submit evidence regarding the problems with Google's proposal, let alone the viability of the Board's pairing of uncapped total content costs with significantly increased total content cost and revenue rates." *Johnson*, 969 F.3d at 383; *see also id.* at 381 ("[T]he Streaming Services argue[ ] they 'had no notice or opportunity to present evidence' about that rate structure because 'no party advocated [it] during or before the hearing.' . . . We agree. *There is no dispute that before and throughout the evidentiary hearing, no party had proposed or even hinted at the structure the Board ultimately adopted*—an uncapped total cost content prong combined with significantly increased rates." (emphasis added)).

The Copyright Owners' naked speculation that, but for Google's proposal, the Board would have adopted a per-play or per-user rate structure fares no better. *See* Copyright Owners' Br. 43-46.[14] The Majority's decision to reject a usage-based metric was not "founded on the

[14] The Copyright Owners ignore that the primary motivation for Google's post-hearing proposal was not to provide an alternative approach for dealing with revenue deferment, but instead was to address "concerns" the panel voiced "over the breadth and complexity of the existing § 115 rates and terms." Google PFF ¶ 56. As noted in the Services' opening brief, the vacated rate structure, which deviates from Google's post-hearing proposal in key respects, does not actually

adoption of the 'true' [uncapped] TCC prong as a backstop against revenue diminution," as the Copyright Owners claim without any supporting citation. Copyright Owners' Br. at 46. To the contrary, the Board "conclude[d] that a flexible, revenue-based rate structure is the most efficient means of facilitating beneficial price discrimination in the downstream market" and, on that basis, rejected "the per-play/per-user rate structures proposed by the Copyright Owners." *Phono III*, 84 Fed. Reg. at 1934.

In any event, this argument is irrelevant to this remand proceeding. Both the Copyright Owners and the Services are now proposing percentage-of-revenue rate structures (albeit with certain critical differences, including very different rate levels). Whatever caused the Judges to reject the Copyright Owners' original per-play/per-subscriber rate structure is no longer at issue here. If the Copyright Owners had concerns with the Judges' rejection of their preferred rate structure, they should have addressed that as part of their appeal to the D.C. Circuit. Having failed to do so, the Copyright Owners cannot now complain that, had it not been for Google's post-hearing proposal, their preferred rate structure would have been adopted. *Crocker v. Piedmont Aviation, Inc.*, 49 F.3d 735, 739 (D.C. Cir. 1995) ("[A] legal decision made at one stage of litigation, unchallenged in a subsequent appeal when the opportunity to do so existed, [governs] future stages of the same litigation, and the parties are deemed to have waived the right to challenge that decision at a later time.").

"reduce the Rube-Goldberg-esque complexity and impenetrability" of the *Phonorecords II* structure, as the vacated structure retains distinctions between multiple different types of statutory services and has rates that vary with the different service types. Services' Br. at 62-63.

2. The Copyright Owners' Argument that the Major Record Labels Do Not Have Market Power Is Waived and Incorrect

The Copyright Owners next argue (at 56-60) that the major record labels do not have complementary oligopoly power over the Services, despite the Majority, Judge Strickler, and the D.C. Circuit all reaching the opposite conclusion. The Copyright Owners have waived this argument, which, in any event, is meritless.

The Judges (both the Majority and Judge Strickler) concluded that the major labels have substantial complementary oligopoly power over the Services, and the D.C. Circuit agreed. *See, e.g.*, *Phono III*, 84 Fed. Reg. at 1933, 1940, 1952-53; *Phono III*, 84 Fed. Reg. at 1964, 2005-06 (Dissent); *Johnson*, 969 F.3d at 382 ("As the Board acknowledges, sound recording rightsholders have considerable market power vis-à-vis interactive streaming service providers, and they have leveraged that power to extract excessive royalties."). The Copyright Owners had the opportunity to timely appeal this determination, but they chose not to.[15] As the D.C. Circuit has repeatedly instructed, "'where an argument could have been raised on an initial appeal,'" it is subsequently "'inappropriate to consider.'" *United States v. Philip Morris USA*, 2015 WL 11198548, at *2 (D.D.C. May 28, 2015) (quoting *Nw. Ind. Tel. Co. v. FCC*, 872 F.2d 465, 470 (D.C. Cir. 1989)); *see also Crocker*, 49 F.3d at 739. The Copyright Owners have identified no reason for undermining the "efficiency and fairness values served by exhaustion principles" and do not deserve a "second bite[] at the apple." *Nw. Ind. Tel. Co.*, 872 F.2d at 471.

Setting aside that the Copyright Owners have waived this argument, the Copyright Owners' efforts to demonstrate that the major record labels do not have complementary

[15] The Copyright Owners contemplated doing so, *see* Appellant Copyright Owners' Preliminary Statement of Issues ¶¶ 1-2, *Nat'l Music Publishers' Ass'n v. Libr. of Cong.*, No. 19-1062 (D.C. Cir. Apr. 12, 2019), but ultimately decided to only appeal the treatment of mechanical floors for student and family plans (an appeal the Copyright Owners lost).

oligopoly power are meritless. The Copyright Owners first assert (at 57) that "not a single service introduced a single scrap of evidence to support the argument" that the major labels form a complementary oligopoly. That is incorrect. The Services introduced substantial evidence on this very issue—evidence that the Judges cited and wove into their decision-making. *See, e.g.*, *Phono III*, 84 Fed. Reg. at 1940; *Phono III*, 84 Fed. Reg. at 2005 (Dissent). Specifically, the economic experts for the Services not only provided the economic logic explaining the source of the major labels' market power and why the Services are subject to that market power, but also pointed to determinations from both the Judges and the Federal Trade Commission embracing this logic and reaching the same conclusion. *See, e.g.*, Ex. 1069 ¶¶ 80-83, 137-141 (Marx WRT); Ex. 886 ¶¶ 56-60 (Katz CWRT); Ex. 698 ¶ 24 (Leonard WRT).[16] In addition, as Professor Marx reinforced at her recent remand deposition, her Shapley Value model also provides support for the conclusion that the major labels wield significant market power over subscription interactive services. Ex. C, Marx Remand Dep. Tr. 39:11-25 ([redacted]).

[16] Several of the Copyright Owners' own experts appear to agree that the labels have substantial market power over the Services. Professor Watt, for example, took the position that it is the record labels that are "[redacted]." 3/27/17 Tr. 3089:19-20 (Watt). And Professor Gans suggested that the burden of the Majority's rate structure and levels "will fall on the services, not the record companies." *Phono III*, 84 Fed. Reg. at 1966-67 (Dissent).

The Copyright Owners next point to a handful of agreements in support of their claim that labels do not have market power. This argument fares no better. The "Subpart A" agreement to which the Copyright Owners point (at 57-58) is one between record labels and music publishers. Whether record labels have market power over the publishers has no bearing on the question whether record labels have market power over the *Services*.

The Copyright Owners also point to certain agreements between [redacted]

3. The Use of Uncapped TCC Prongs for Less Economically Consequential Offerings Has No Bearing on Whether the TCC Prong for Subscription Interactive Services Should Be Capped

The Copyright Owners' final effort to muddy the waters is to argue again that an uncapped TCC prong for subscription interactive services must be reasonable because the Services proposed maintaining uncapped TCC prongs for certain less economically consequential products. Copyright Owners' Br. at 50-54. But the D.C. Circuit already rejected this argument, concluding that "the fact that some of the Streaming Services' proposals contemplated continued use of an uncapped total content cost prong for a small number of preexisting categories does not mean that the Board would uncap the total content cost prong across the board. *That is quite different*." *Johnson*, 969 F.3d at 382 (emphasis added).

Moreover, the economic risks associated with an uncapped TCC prong for subscription interactive services are fundamentally different from those associated with certain other product offerings. The subscription interactive service offerings generate the large majority of interactive streaming revenues. Subjecting those offerings (and their revenues) to the unchecked market power of the record labels poses very different risks to the Services than subjecting less consequential offerings to the market power of the labels.

There are also practical difficulties with implementing a per-subscriber cap on the TCC prong for certain products, like ad-supported services and bundles, because there can be challenges in defining a "subscriber." *See, e.g.*, Ex. C, Marx Remand Dep. Tr. 21:17-22:9 (explaining that [redacted]).

Finally, the Services' rate proposal is derived in large part from the *Phonorecords II* settlement, which, by its very nature, embodied a compromise. The services in *Phonorecords II* acceded to unfavorable terms on certain offerings with more limited (or no) impact on their revenue as part of a broader compromise that included capped rates for their most significant offerings. By proposing to continue the use of capped TCC prongs for certain offerings and uncapped TCC prongs for others, the Services simply seek to maintain the bargain struck between the Copyright Owners and the Services (including those aspects that benefit the Services and those that do not). The Copyright Owners, on the other hand, seek a significant departure from that compromise that would leave the flagship offerings of the "Streaming Services exposed to potentially large hikes in the mechanical license royalties they must pay" by "yok[ing] the mechanical license royalties to the sound recording rightsholders' unchecked market power." *Johnson*, 969 F.3d at 382. The Copyright Owners offer no justification for that dramatic departure from a time-tested bargain.

For all these reasons, and for those set forth in the Services' opening brief, the Judges should reject the Copyright Owners' efforts to have the vacated rate structure and rate levels reinstated.

IV. THE JUDGES SHOULD RETAIN THE INITIAL DETERMINATION'S DEFINITION OF SERVICE PROVIDER REVENUE

A. The Copyright Owners Do Not Identify Any Legal Authority Allowing for Substantive Modifications to the Initial Determination's Service Provider Revenue Definition

Resolving the remanded question with respect to the Service Provider Revenue definition for bundles both starts and ends with a threshold issue: whether the Judges have the *legal authority* to substantively modify the Initial Determination's definition. As the Services demonstrated in their opening brief, the D.C. Circuit effectively ruled out each of the three sources of statutory authority for making such a modification, and no others exist. *See* Services' Br. at 64-68. The Copyright Owners contend in a footnote that the Judges can simply reassess the Initial Determination's Service Provider Revenue definition on remand while ignoring the threshold question of its authority to make such a modification. This position is meritless and fails to come to grips with the Copyright Act, *Johnson*, and the Judges' own prior findings.

The Copyright Owners first suggest (at 73-74) that, on remand, the Judges need not respond to the error the D.C. Circuit identified with this aspect of the Final Determination: the Judges' "fail[ure] to explain the legal authority for [their] late-breaking rewrite" of the Service Provider Revenue definition. *Johnson*, 969 F.3d at 389. But "an agency's review on remand must be responsive to the court's mandate." *Bean Dredging, LLC v. United States*, 773 F. Supp. 2d 63, 78 (D.D.C. 2011) (citing *Process Gas Consumers Grp. v. FERC*, 292 F.3d 831, 840 (D.C.

Cir. 2002)). And failing to respond to the reviewing court's mandate will result in a second remand. That is what happened in *Ali v. Pompeo*, where the reviewing court remanded *again* after the State Department on remand adopted, based on the same record, an alternative ground for the same result it had reached earlier—but did not address the issues on which its initial decision was remanded. 2020 WL 6435834, at *5 (E.D.N.Y. Nov. 2, 2020). The State Department's failure to address the legal and factual issues on which the court remanded "violate[d] th[e] Court's prior order." *Id.* The Judges are similarly bound to answer the remanded question here.

The obligation to address remanded questions and follow the reviewing court's mandate is particularly important in this context, where the D.C. Circuit recognized that the Copyright Act places limits on the Judges' authority to alter an initial determination by defining the conditions for rehearing and the types of changes that are permitted absent a rehearing. Those "limit[s]" would improperly be rendered a "nullity," *Johnson*, 969 F.3d at 392, if the Judges were free to use the remand as an opportunity to make changes not allowed following the Initial Determination. The Judges cannot do on remand what they lacked authority to do in the first instance, and they must resolve the legal question whether there is authority to alter the revenue definition in the Initial Determination.

Consistent with the distinct procedural history of the Service Provider Revenue definition, the D.C. Circuit's remand does not give the Judges the authority to bypass the remanded question and simply re-do the *Initial* Determination with regard to that definition. In contrast, on the other remanded issues—the rate levels and rate structure for the statutory license—the D.C. Circuit specifically identified errors in the Initial Determination that the Judges must address. *See Johnson*, 969 F.3d at 383, 387. But the error the D.C. Circuit identified with the Service Provider Revenue definition was *not* in the Initial Determination; it was an error contained only in the Judges' Rehearing Order and Final Determination. *See id.* at 392. Therefore, the remanded issue is not what the substance of the Service Provider Revenue definition should be as a matter of first impression—it is instead whether the Judges may *alter* the Initial Determination's definition. Only after answering that threshold question in the affirmative could the Judges then address the substance of the Service Provider Revenue definition.

The remand gives the Judges two paths to answering that threshold question: provide a "fuller explanation" of the prior conclusion that the Judges had legal authority to revise the Service Provider Revenue definition in the Initial Determination or answer that threshold question through "new agency action." *DHS v. Regents of the Univ. of Cal*., 140 S. Ct. 1891, 1907-08 (2020). When following the "fuller explanation" path, the Judges are limited to elaborating on what they said previously; they cannot, for instance, add new reasons they did not initially provide. *See id.* In contrast, the "new agency action" path gives the Judges freedom to consider new reasons for (or against) the conclusion they previously reached—namely, that the Copyright Act provided the Judges with the authority to make this change to the Initial Determination. *See id*. But undertaking a new agency action does not, as the Copyright Owners claim (at 72), obviate the need for the Judges to identify proper legal authority before substantively changing the Initial Determination. *See*, *e.g.*, *Fisher v. Pension Benefit Guar. Corp.*, 994 F.3d 664, 670 (D.C. Cir. 2021) (finding that the agency properly engaged in new agency action on remand where it addressed its legal authority by adopting an argument it had not considered in the initial proceeding).

The Copyright Owners argue (at 71 & n.33) that the Judges may use the "fuller explanation" option to invoke the technical correction authority of Section 803(c)(4) or the rehearing authority of Section 803(c)(2). As the Copyright Owners effectively admit by relegating it to a footnote, this argument is not serious. The "fuller explanation" path on remand allows an agency to "elaborate" on its "initial explanation" for its action—but it "may not provide new ones." *Regents*, 140 S. Ct. at 1908.

The Judges did not rely on Section 803(c)(4) in the Final Determination, *see Johnson*, 969 F.3d at 391, which means that invoking it now would plainly be a new reason, not an elaboration on prior reasoning. *See Ali*, 2020 WL 6435834, at *8-9 (holding that, where State Department "relied on the same factual basis . . . to reach the same result . . . , but it has substituted a different legal justification," it impermissibly "invok[ed] post hoc rationalizations"). Reliance on Section 803(c)(2) rehearing authority is even more clearly barred, because the Judges "specifically disavowed" that the rehearing standard was satisfied or that they were exercising their rehearing authority. *Johnson*, 969 F.3d at 390. Such a "*volte-face*" is foreclosed on remand just as it was on appeal. *Id.* The Judges' correct and unappealed determination that the Copyright Owners had not satisfied the "exceptional cases" standard for rehearing, 17 U.S.C. § 803(c)(2)(A), remains binding as the law of this case. *See Duberry v. District of Columbia*, 924 F.3d 570, 579 (D.C. Cir. 2019); Services' Br. at 65-66. Moreover, the Judges cannot exercise their rehearing authority in this remand because the Copyright Owners did not seek rehearing, *see Johnson*, 969 F.3d at 390, and Section 803(c)(2) allows rehearing only "upon motion of a participant," 17 U.S.C. § 803(c)(2)(A).

Finally, the Copyright Owners assert (at 74) that the D.C. Circuit would have reversed instead of remanding if the only possible outcome was for the Judges to reinstate the Initial

Determination's definition. That claim mischaracterizes both the D.C. Circuit's practice and the Services' argument. The D.C. Circuit will reverse only "[i]n rare circumstances, when a remand would be futile." *Fisher*, 994 F.3d at 669. The court in *Johnson* could not reverse because the Department of Justice raised new justifications for the Majority's decision to change the Initial Determination for the first time on appeal. Under basic administrative law principles, which the D.C. Circuit invoked throughout *Johnson*, a reviewing court "cannot rely on" "arguments by counsel [that] are nowhere to be found in" the agency's decision "to sustain that decision." 969 F.3d at 387. Therefore, the D.C. Circuit could not assess whether those novel rationales provided the Judges with authority to change the Initial Determination. *See id.* at 391 ("[W]e may not sustain the Board's action based on its attorney's theorizing at oral argument."); *id.* at 392 (refusing to review the "equivocal" claims of "plenary authority to revise its [initial] determinations" that counsel raised at oral argument). Instead, the court had to remand and give the Judges the opportunity to address the Department of Justice's new justifications in the first instance, as the D.C. Circuit could not rule them out given the posture of the appeal. But the statutory scheme, the D.C. Circuit's holdings, and the court's reasoning all make clear that the Department of Justice's belatedly raised justifications also fail. There is no potential source of legal authority that can justify the Judges' late, substantive change of the Initial Determination's Service Provider Revenue definition. *See* Services' Br. at 64-68.

In short, the threshold question the D.C. Circuit's remand poses is whether the Judges have authority to substantively change the Initial Determination's Service Provider Revenue definition. For the reasons above and in the Services' opening brief, no such authority exists. Therefore, the Judges' need not and should not address the substantive merits of the Initial

Determination's definition and the Copyright Owners' belatedly proposed alternatives. In any event, as explained below, the record amply supports the Initial Determination's definition.

B. On the Existing Record, the Judges Should Not and Cannot Modify the Service Provider Revenue Definition

The record evidence on bundles shows that the Service Provider Revenue definition the Services proposed and the Initial Determination retained is both supported by the *Phonorecords II* benchmark and has proven, industry-wide benefits. *See* Services' Br. at 68-75. The Copyright Owners, in contrast, did not propose an alternative definition of Service Provider Revenue until *after* the Judges issued the Initial Determination, and the alternatives they propose now have no basis in the written record. *See id.* at 75-76. Where the choice is between some evidence and none, "something outweighs nothing every time." *Covad Commc'ns Co. v. Bell Atl. Corp.*, 407 F.3d 1220, 1222-23 (D.C. Cir. 2005) (ellipsis omitted) (quoting *Nat'l Ass'n of Retired Fed. Emps. v. Horner*, 879 F.2d 873, 879 (D.C. Cir. 1989)).

The Copyright Owners' arguments misconstrue the record, the economics, and the procedural history. In large part, the Copyright Owners repeat points they made after the Initial Determination, and the Judges have already correctly determined that the record evidence identified by the Copyright Owners does not support their proposed alternative definitions. *Compare* Copyright Owners' Mot. for Clarification or Correction at 11-13, *Phono III*, No. 16-CRB-0003-PR (2018-2022) (Feb. 12, 2018), eCRB Doc. No 2026 (Mot. for Clarification).

1. The Copyright Owners' key example (at 85-86) of the purported unfairness of the existing Service Provider Revenue definition actually shows the opposite—it shows why the existing definition works for bundles. As the Copyright Owners note, between July 2014 and December 2016, [redacted]

[redacted] Ex. 132 ¶¶ 2.22, 3.9 (Hubbard WRT). The Copyright Owners complain that these new users used Prime Music more and so the number of streams grew even faster than royalties grew. But that comparison is irrelevant, as the Judges roundly rejected the Copyright Owners' per-stream proposal for mechanical royalties. *See Phono III*, 84 Fed. Reg. at 1934. The rejected per-stream metric provides no basis to reassess the suitability of the Initial Determination's Service Provider Revenue definition.

In addition, as Dr. Hubbard explained, it is "meaningless" to compare growth in streams to growth in royalties in the context of Prime Music in particular because the record showed that Prime Music brings "new people into the market." 4/13/17 Tr. 6006:10-13 (Hubbard). If not for the flexibility (and beneficial price discrimination) the existing Service Provider Revenue definition and rate structure facilitated, the Copyright Owners "would have gotten zero" from those new listeners. *Id.* at 6006:13-14. "So they're better off by that amount" of royalty growth. *Id.* at 6006:14. The undisputed fact that royalties grew faster than users—even as users skyrocketed—reflects that the existing rule enables beneficial price discrimination that expands the total royalty pool and benefits Copyright Owners.[17] And the evidence of Prime Music's

[17] The Copyright Owners claim (at 83) that [redacted] This assertion badly misconstrues Dr. Hubbard's testimony. At the hearing, the Copyright Owners' counsel asked Dr. Hubbard about the different royalty minima for stand-alone services (50 cents per subscriber) and bundled services (25 cents per active subscriber) in the *Phonorecord II* settlement. The Copyright Owners clarified that their "question was do you have understanding of where that difference came from." Dr. Hubbard answered: "I don't. I'm sorry. I'm not an attorney." 4/13/17 Tr. 5991:11-14. That testimony is not, as the Copyright Owners now assert, an admission that there is no economic rationale for having a lower royalty minimum for bundles than for stand-alone services. Indeed, the economic rationale—enabling flexibility to capture low willingness-to-pay listeners who would not

power to funnel users into stand-alone paid services means that Prime Music expands the royalty pool even further. Ex. 111 ¶ 39 (Mirchandani WRT). In their repeated complaints about Prime Music, the Copyright Owners ignore this evidence entirely.[18]

The Copyright Owners also discuss (at 89-90) some of [redacted] actual and contemplated bundles, which reflects that bundling does and will continue to offer attractive economics to consumers. The actual and contemplated bundles discussed in the record all demonstrate the value of flexibility and the benefits of price discrimination. Not only is the existing Service Provider Revenue definition the only definition supported by the record; it is also the only option under consideration that protects that flexibility without creating the potential for administrative complexity. *See* Services' Br. at 75-76. Nor are the Copyright Owners correct (at 77) that Dr. Marx "essentially conceded the inappropriateness of the prior definition in light of the economic indeterminacy issue." The transcript pages they cite say nothing of the sort—nothing about bundles, nothing about economic indeterminacy, and certainly nothing about [redacted] (or any Service's) proposal being inappropriate. Dr. Marx there testified only that she did not have an expert opinion on the rate proposal as a whole because she had not analyzed the rate proposal as a whole. 4/7/17 Tr. 5602:20-5605:1.

2. The Copyright Owners (at 81-82) again propose two approaches for the Judges to consider in addressing the substance of the Service Provider Revenue definition as applied to bundles: either adopting a definition encompassing "all of the revenue attributable [to] the bundle" or adopting the same rule the Majority included in the Final Determination. Each of

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otherwise pay for music—is straightforward and was reaffirmed by Dr. Hubbard and others. *See* Services' Br. at 68-75; Ex. 132 ¶ 2.7 & n.18 (Hubbard WRT).

[18] The evidence that Amazon successfully uses Prime Music to funnel users to its Music Unlimited service refutes the Copyright Owners' claim (at 85-87) that the record evidence shows that Prime Music is a large source of Amazon profits.

these approaches would cause a net loss by discouraging beneficial price discrimination through bundling—a point the Copyright Owners do not, and cannot, deny.

Basing Service Provider Revenue on all the revenue attributable to the bundle would, of course, ignore the value of the non-music components of the bundle. Those non-music components can exceed the value of the music component and—as in the case of Prime—can exceed the full price of the bundle itself. *See* Services' Br. at 73.[19] Attributing the entirety of the bundle's revenue as Service Provider Revenue would create an overwhelming incentive to discontinue bundles and to shutter innovative services such as Prime Music entirely, even though the record showed that bundles grow the royalty pool.

And both of the Copyright Owners' proposed approaches ignore the basic purpose of bundling—to offer *discounts* from stand-alone prices to attract customers unwilling to pay full price for each of the services included in the bundle. Bundling thus enables beneficial price discrimination that the Judges rightly sought to protect. *See* Services' Br. at 68-75. Moreover, basing Service Provider Revenue on the music component's stand-alone price will create significant administrative and auditing complexities for services like Prime Music that are not offered or priced on a stand-alone basis.

3. The Copyright Owners' assertion (at 78-81) that a party bears the burden to justify its proposed rule cuts against the Copyright Owners—they are the parties that failed to meet any such burden. The Services expressly proposed a Service Provider Revenue definition

[19] The Copyright Owners imply (at 76, 80, 84) that Services have abused the Initial Determination's method for calculating Service Provider Revenue by "[redacted]." But whether Services' [redacted]. The rule instructed Services to deduct the stand-alone *prices* of non-music components, and that was precisely what they did. *See* 3/16/17 Tr. 1483:3-1484:1 (Mirchandani).

and supported it with evidence that this definition, which was voluntarily agreed to and already in use, had led to and would continue to lead to a widely beneficial expansion of the royalty pool. It is simply not true, as the Copyright Owners assert (at 80), that the Services "provided no evidence explaining where the definition came from [or] how it operated in practice." *Compare* Services' Br. at 69-74 (summarizing record evidence).[20] Meanwhile, it was the Copyright Owners, as the Judges recognized, that "did not present evidence to support a different measure of bundled revenue because their rate proposal was not revenue-based" and instead attempted to rely on "the evidentiary records in *Web IV* and *SDARS III* [that] differ from the record in this proceeding." Order Granting in Part and Denying in Part Motions for Rehearing (Amended) at 17-18, *Phono III*, No. 16-CRB-0003-PR (2018-2022), eCRB Doc. No. 3602 (Jan. 4, 2019) (Rehearing Order). The Copyright Owners have not satisfied—and, given the Judges' prior reasoning and the closed record on remand, cannot be found to have satisfied—their burden of justifying the Service Provider Revenue definitions they now propose.[21]

[20] Nor is there any rule requiring that a participant explain from where a proposed definition came. The Copyright Owners cite to no such rule.

[21] The evidence identified now by the Copyright Owners is the same evidence that they relied on in their Motion for Clarification. *See* Mot. for Clarification at 12-13 (citing Copyright Owners' COL ¶¶ 364, 365). The Judges correctly held that this evidence did not support the Copyright Owners' proposed rule, which is why the Judges decided the Service Provider Revenue definition "[b]y default." Rehearing Order at 18. Such decisions made "by default" based on a purported evidentiary vacuum are unlawful and have been repeatedly reversed by the D.C. Circuit. *See Intercollegiate Broad. Sys.*, 574 F.3d at 767; *Settling Devotional Claimants v. Copyright Royalty Bd.*, 797 F.3d 1106, 1121-22 (D.C. Cir. 2015). The Services raised this "by default" error on appeal, and *Johnson* did not reach the issue only because the court vacated on the threshold issue of the Judges' legal authority. *See Johnson*, 969 F.3d at 392 ("Because the Board failed to identify any legal authority for adopting the new Service Revenue definition, we have no occasion to address the Streaming Services' separate argument that the definition was arbitrary, capricious, or unsupported by substantial evidence."). It would be reversible error for the Judges to again select a different Service Provider Revenue definition "by default."

The Copyright Owners also repeat (at 75-78) their erroneous argument that *Web IV* and *SDARS III* adopt a rule that requires resolving all bundling issues against licensees because of the economic indeterminacy inherent in bundling. The discussion in *Web IV* about "ice cream cones" and "tires" that the Copyright Owners quote (at 76) was about whether marginal or average pricing was the right way to assess a deal where the seller's willingness to offer more of the *same* items resulted in a lower per-item price for the additional units. That discussion had nothing to do with the pricing of bundles containing *distinct* goods. Therefore, the Judges' decision in *Web IV* to calculate the value of a benchmark deal involving a single product using average, rather than marginal, pricing says nothing about how to value bundles. It certainly does not adopt a rule that disputes about the valuation of components of bundles must always be resolved against the seller of the bundle.

In contrast, the Judges' decision in *SDARS III* did involve valuation of the music and non-music components of a bundle. But, as Judge Strickler already explained, the resolution in *SDARS III* is inapposite because, here, the rate structure has a way of ensuring that Copyright Owners are fairly compensated from bundles: the statutory minimum payment. *See* Services' Br. at 75-76 (citing *Phono III*, 84 Fed. Reg. at 1992 n.266 (Dissent)). As illustrated above, those minimum royalty payments were why [redacted]. That is powerful evidence that the Initial Determination's Service Provider Revenue definition (which enables innovative bundles) combined with the minimum royalty (which ensures Copyright Owners share in the gains from that innovation) strikes the right balance in managing the uncertainty inherent in valuing components of bundles.

Because the Judges cannot lawfully alter the existing Service Provider Revenue definition—and because the record in any case supports retaining it—the Initial Determination's Service Provider Revenue definition should be retained.

CONCLUSION

For these reasons and those stated in the Services' Joint Opening Brief, the Board should adopt the Services' Proposal in its entirety.

July 2, 2021

Respectfully submitted,

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Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
The Library of Congress
Washington, D.C.

In re **DETERMINATION OF ROYALTY RATES AND TERMS FOR MAKING AND DISTRIBUTING PHONORECORDS (Phonorecords III)**	**Docket No. 16-CRB-0003-PR (2018-2022) (Remand)**

DECLARATION OF AARON J. CURTIS
IN SUPPORT OF SERVICES' JOINT REPLY BRIEF

(On behalf of Amazon.com Services LLC, Google LLC, Pandora Media, LLC, and Spotify USA Inc.)

1. I am counsel for Pandora Media, LLC in the above-captioned case. I respectfully submit this declaration on behalf of Amazon.com Services LLC, Google LLC, Pandora Media, LLC, and Spotify USA Inc. (collectively, the "Services"). I am authorized to submit this declaration on the Services' behalf.

2. Attached as Exhibit A to the Services' Joint Reply Brief is a true and correct copy of the final transcript of Michael L. Katz's deposition in this proceeding, held on June 8, 2021.

3. Attached as Exhibit B to the Services' Joint Reply Brief is a true and correct copy of the final errata sheet submitted by Michael L. Katz in connection with his deposition in this proceeding, held on June 8, 2021.

4. Attached as Exhibit C to the Services' Joint Reply Brief is a true and correct copy of the final transcript of Leslie Marx's deposition in this proceeding, held on June 2, 2021.

5. Attached as Exhibit D to the Services' Joint Reply Brief is a true and correct copy of the final errata sheet submitted by Leslie Marx in connection with her deposition in this proceeding, held on June 2, 2021.

Pursuant to 28 U.S.C. § 1746, I hereby declare under the penalty of perjury that, to the best of my knowledge, information, and belief, the foregoing is true and correct.

Dated: July 2, 2021
New York, NY

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Exhibit A
[REDACTED]

Exhibit B
[REDACTED]

Exhibit C
[REDACTED]

Exhibit D
[REDACTED]

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
The Library of Congress
Washington, D.C.

In re **DETERMINATION OF ROYALTY RATES AND TERMS FOR MAKING AND DISTRIBUTING PHONORECORDS (Phonorecords III)**	**Docket No. 16-CRB-0003-PR (2018-2022) (Remand)**

DECLARATION AND CERTIFICATION OF AARON J. CURTIS REGARDING RESTRICTED PROTECTED MATERIAL

(On behalf of Amazon.com Services LLC, Google LLC, Pandora Media, LLC, and Spotify USA Inc.)

1. I am counsel for Pandora Media, LLC in the above-captioned case. I respectfully submit this declaration and certification pursuant to the terms of the Protective Order issued July 27, 2016 (the "Protective Order"). I am authorized by Amazon.com Services LLC, Google LLC, Pandora Media, LLC, and Spotify USA Inc. (collectively, the "Services") to submit this declaration on their behalf.

2. I have reviewed the Services' Joint Reply Brief (the "Reply Brief") and Exhibits A-D thereto. I have determined that portions of the Reply Brief contain information that the Participants previously designated as "Restricted" under the Protective Order when that information appeared in documents and/or prior filings submitted in this proceeding (the "Protected Material"). Exhibits A-D constitute deposition transcripts that have, by agreement of the Participants, been designated as "Restricted" in their entirety. The Protected Material is shaded in grey highlight in the restricted e-filings of the Reply Brief, and is fully redacted in the public e-filing of the Reply Brief. In addition, Exhibits A-D are filed under seal in accordance with Section IV.A of the Protective Order.

3. The Protected Material includes, but is not limited to, testimony and exhibits involving (a) contracts and contractual terms (including the negotiation thereof) that are not available to the public, highly competitively sensitive and, at times, subject to express confidentiality provisions with third parties; and (b) highly confidential internal business information, financial projections, financial data, negotiation correspondence, and competitive strategies that are proprietary, not available to the public, and commercially sensitive.

4. If this contractual, strategic, and financial information were to become public, it would place the Services at a commercial and competitive disadvantage, unfairly advantage other parties to the detriment of the Services, and jeopardize their business interests. Information related to confidential contracts or relationships with third-party content providers could be used by the Services' competitors, or by other content providers, to formulate rival bids, bid up Service payments, or otherwise unfairly jeopardize the Services' commercial and competitive interests.

5. The contractual, commercial, and financial information described in the paragraphs above must be treated as Restricted Protected Material in order to prevent business and competitive harm that would result from the disclosure of such information while, at the same time, enabling the Services to provide the Copyright Royalty Judges with the most complete record possible on which to base their determination in this proceeding.

Pursuant to 28 U.S.C. § 1746, I hereby declare under the penalty of perjury that, to the best of my knowledge, information, and belief, the foregoing is true and correct.

Dated: July 2, 2021
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Proof of Delivery

I hereby certify that on Friday, July 02, 2021, I provided a true and correct copy of the SERVICES’ JOINT REPLY BRIEF (Public) to the following:

Johnson, George, represented by George D Johnson, served via ESERVICE at george@georgejohnson.com

National Music Publishers' Association (NMPA) et al, represented by Benjamin Semel, served via ESERVICE at Bsemel@pryorcashman.com

Nashville Songwriters Association International, represented by Benjamin K Semel, served via ESERVICE at Bsemel@pryorcashman.com

Signed: /s/ Todd Larson